

# Draft Reform Proposals



Social Protection Reform Project  
中国-欧盟社会保护改革项目

## COMPONENT ONE

### Macro-activity 1.6

#### 2015 programme of activities

##### PENSION SYSTEM

Into the Chinese XIIIth Five-year Plan

Social insurance administration

Combining Social pooling & Individual accounts

Designing a multi-tier pension system

Public sector pension reform

Integrating Urban and Rural social security protection

June 2016

## Foreword

As part of the EU-China Social protection reform project 2015 Programme of activities, a workshop was held in Beijing on 21 January 2016 to debate the situation analysis produced by Chinese experts on the five topics under review that year, notably in the light of most relevant European best practices documented in a special consolidated report, and in the light of the provisions proposed for inclusion in the relevant chapter of the XIIIth Five-Year plan.

According to the Project Grant application form macro-activity 1.6 the Workshop focused on “the first draft of reform proposals related to the topics analyzed”. The present document presents these draft reform proposals as tabled at the Workshop meeting, organised according to the results pursued by the project.

The Assessment report containing the integrity of related analysis report, summary of discussions and presentation of most relevant European best practices can be downloaded from <http://www.sprp-cn.eu/reporting.htm> in printable format. Individual contributions and the Workshop report are also accessible from the project website, <http://euchinasprp.eu>.

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June 2016.

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## **PROJECT RESULT 2**

### **Improved Inter-agency Cooperation in social protection reform**

## Topic 1.1.1 (revised)

Contributing to the Elaboration of the XIIIth National Five Year Plan (2016-2020)<sup>1</sup>

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<sup>1</sup> Excerpt from report by Chinese expert Mr. Tan Zhonghe

According to the development target and basic principles for social security during the 13th five-year period, the main contents of social security reform are as follows:

### **Further improve retirement pension system**

#### *1. Promote urban and rural old-age insurance in a coordinated way to achieve a full coverage*

Coverage rate is one of the basic measures to evaluate the effectiveness of the old-age insurance system. It is also the important task for China. Now the coverage rate for the developed nations in Europe and the US is around 90%. By 2020, China's total population will reach 1.434 billion. The basic old-age pension system should cover 1.05 billion. Targeting the 95% coverage rate, it should reach 1 billion people (workers basic endowment insurance 440 million people and residents' old-age insurance 560 million people). Among them, people entitled for basic old-age insurance should be 286 million (workers basic old-age insurance 126 million and residents' old-age insurance 160 million). Now the basic old-age insurance has covered 840 million people. To achieve a full coverage, it should cover another 160 million people in the future 5 years. Among them, workers basic old-age insurance should at least add 110 million. Considering 40 million staff at governmental and public organizations incorporated into workers basic pension system, at least 10 million should be added each year. Urban and rural old-age insurance system should add 50 million in total, and 10 million each year.

Regarding the difficulties for a full coverage, in towns, it falls on the migrant workers, internet economy employees, housekeeping personnel, self-employed people and the handicapped. Most of them work in non-public sector and micro businesses. Due to its small economic scale, flexible operational model and instable employment and low income, they lack the ability to pay for the premium. In rural areas, it mainly falls on young people who don't have the willingness to pay and some poor people who don't have the ability to pay. Targeting the conditions above, we should gradually incorporate qualified people into the system by combing law enforcement and interest's orientation, and policy improvement and promotion.

#### *2. Improve insurance policy for residents and self-employed people*

We should further improve incentive mechanism of paying premium more and getting insured more, to mobilize the individually employed businesspeople, flexibly employed people and urban and rural residents to get insured. For residents who choose high-end premium and for a longer-period premium, we could appropriately increase government subsidy and give additional basic pension, guide by interests and step up insurance management to encourage consistent and longer premium. For the people living on minimum subsistence allowances and the handicapped, we should improve the policy of government supported payment. Targeting the prominent issue of suspending premium by the low-income group and flexibly employed people, we should improve the statistical methods of social average salary, by including that of the private companies into calculation. Thus it could lower the payment base and increase the premium elastic range, by expanding the base from 60% to 300% of social salary, thus keeping consistent with enterprises workers premium range and facilitating them to choose how much to pay according to their own conditions.

### *3. Improve connection method of endowment insurance*

At present, the policy of interprovincial transfer of workers basic pension and connection of workers basic old-age insurance and rural and urban residents social endowment has been carried out steadily. It solve the problem for transregional transfer of workers insurance (including migrant workers) and the connection between workers and residents insurance. But in actual condition, they still face difficulties in transfer and connection and the high cost for the move and some of them even cannot transfer their insurance. We should speed up unifying operation process for transfer and connection and improve the nationwide unified information system of social security to curb enjoying repeated insurance and standardize and computerize transfer and connection to provide convenient service for insured people.

### *4. Improve individual account system of basic old-age insurance for urban workers*

At the beginning of the century, the state council of China, while creating social security strategic reserve fund, was determined to carry out pilot of consolidating workers basic old-age insurance individual account to accumulate partial fund for future. Evaluating on the more than 10-year operation, these measures are of important strategic significance for coping with ageing of population and alleviate fund payment pressure under future accounting on the cash basis. But consolidating pilot program also faced with prominent problems. Some regions faced great pressure in ensuring current cashing. Companies were heavily burdened. Effective investment channels were lacked to preserve and increase value for consolidating fund. Various regions lack initiative to do it and to continue to expand the fund was faced with severe challenges. We need to adjust policy and make a directional choice. The main purpose of creating individual account was to clarify the old-age insurance responsibility between government and individuals. Only this function was played out, consolidating or not consolidating all can be a choice. It will not affect the basic model of accounting on cash and partial accumulation in general. On the condition that the strategic reserve fund has been created and continued to expand, we can choose not to deposit another sum of money to consolidate it. There have been different views on individual accounts in the international community. The International Labour Organization, and the International Social Security Association consistently oppose the accumulation system of personal savings without the function of mutual aid. The World Bank, previously advocated strongly consolidating individual accounts, but recently it proposed that China could implement individual nominal accounts. Seeing from the different countries' practice worldwide, there are those who took individual accounts, while others nominal accounts. On comprehensive analysis and considering that China can hardly meet the condition to consolidate individual accounts in a long period of time (huge cost in payment system transition and difficulty in achieving good investment return for doing it), China could consider not to continue to consolidate the individual accounts of workers basic old-age insurance, rather it could take individual accounts as an incentive treatment. Suggestions: First, adhere to solid account accumulation for urban and rural residents' old-age insurance individual account. This fund is from individual payment and has not burden of historical debt. It cannot be used for basic pension and must be invested standardized, and keep account according to actual investment earnings. Second, standardize workers' pension individual account interest rate. Due to long-term capital nature of the premium, to maintain the replacement rate of the individual account endowment, the accounting interest rate should be set on comprehensively considering the growth of workers' salaries and the factor of rising of commodities prices. It should be released by the nation annually. All these are to encourage people's incentives to get insured. Third, appropriately cut companies' premium rate and promote supplementary old-age insurance. Workers personal premium will be fully

pooled into coordinated funds to ensure people get insured timely and to alleviate payment pressure for that purpose. Meanwhile, Companies' premium should be cut down appropriately and they are encouraged to use some of the money to build a supplementary pension so as to promote the building of a multi-level security system and reduce the future capital pressure.

5. *Accelerate achieving a nationwide planning of workers old-age insurance on the basis of summarizing province-level planning experience*

Internationally, for the countries practicing a basic old-age insurance system, they all take uniformed system and policy nationwide and uniformed operation of funds. And rarely is there a phenomenon of different regions taking their own policies and managing their own funds. China took a path on which some regions engaged in pilot program at first, and then the country summarized the experience and gradually made it a standardized national policy. It played a positive role for exploring ways, improve policy and ensure people get insured timely at the initial stage. But there were problems such as not uniformed policy, regional segmentation and ambiguity of power and responsibility between central and local governments. At present, half of the balance of funds for workers old-age insurance are concentrated in very few eastern provinces. Different regions have different dependency ratio and premium for the companies, from 13% to 21%. In recent years, as the provincial planning system was put in practice, policy was uniformed and funds can be transferred for use within the province. And stimulus and constraint mechanism for localities by the provinces was also built. All these laid a foundation for nationwide planning. According to the requirement of law of large numbers of social insurance, the objectives of the nationwide planning are to carry out unified system and policy and management process and information system across the country by stepping up central government's decision-making mechanism. The objectives also coordinate the use and management of the funds, balance regional burdens, strengthen the anti-risk capability of the funds and facilitate flow of the people got insured to promote the formation of a unified labour market and fair competitive market environment. The core is to clarify the financing and payment responsibility of the central and local governments on basic old-age insurance fund, clarify power and responsibility and mobilize the incentives of both central and local governments by combining the conditions of present finance management system and regional imbalanced economic development. The planning could consider starting from workers basic old-age insurance and followed by the one of the government and public organizations' staff. The urban and rural residents' old insurance could not meet the condition to incorporate into national planning, because its system is different from the workers' basic old-age insurance, and their financing channels and treatment setting mechanism are also different.

It is not suitable to practice unified collection and allocation of funds by the state for the nationwide planning. We could consider taking partial planning for current funds collection and payment to create central planning funds. Through the adjustment by this fund can we effectively balance burdens between regions and alleviate the problem that in some places they have too much reserves while others lack money for payment so as to promote unified premium rates and leave rooms for reducing employers' rates.

6. *Setting a criterion for financing and social security that commensurate with economic development to avoid insufficient security or excessive security*

Financing and treatment level concerns not only the healthy operation of the old-age insurance but also the economic burden of the employers and the individuals and the basic living condition of the



people got insured. Thereby it affects the social and economic development. Therefore, we should set a criterion for financing and social security that commensurate with economic development.

- i. Adjust properly the premium rates for the organizations in a timely manner

According to the ranking of 164 countries listed in Global Social Security, the sum of premium rate by both the organization and individual reached 28%, ranking the 13th. The rate is relatively high. It is mainly because the companies' old-age insurance premium shoulders the system transition cost and state-owned enterprises reform cost. Because before the system transition, the old people have no individual account accumulation, the middle-aged people have no fund indemnity during the period regarded as payment one and nearly 10 million people retired in advance during the SOEs reform period from 1998 to 2006, current payment mainly relied on payment from companies and individuals. Meanwhile, the low overall planning and imbalanced fund balance reduced the fund use efficiency. The huge gap between premium basis and salary statistics also caused the virtual-high of the premium rate (premium rate which is 20% in 2012, if calculated on the social average salary that included private companies, would be 16%). The relatively high premium rate made the financial burden for companies heavier and constrained the improvement for competitiveness. At the same time, it exacerbated the payment evasion and resulted into a vicious circle. Our studies show that the system transition has not ended yet, the payment for the period regarded as payment one will continue for about 20 years, and as the peak for ageing is coming, the total premium rate has no room for a big down adjustment. Considering such factors as the government will continue to increase subsidy, more people will be get insured, premium salary base will be standardized, structural problem for fund will be solved by national planning and the capital use efficiency will be improved, we could properly adjust the employers' premium rate for old-age insurance. The rate for individuals will not be changed, as 8% is relatively suitable.

- ii. Properly setting the replacement rate of the basic old-age pension

The Social Security (Minimum Standards) Convention (No. 102) by International Labour Organization, which took effect in 1952, stipulates that the minimum old-age allowance for the people got insured for 30 years, should be no less than 40% of their average salary. The new standard in No. 128 Convention in 1967 was 45%. Among the over 160 countries that have old-age insurance system, about 78% of them have a comprehensive replacement rate (basic + supplement) over 60%. The rate for developed countries like France, Germany, Japan, and UK was 62%, 52%, 49% and 47% respectively. Based on the above conditions, we believe that the average replacement rate for the primary treatment is better to keep between 45% and 70% due to the small share of the supplementary insurance in China. The target replacement rate for the urban and rural residents' pension should be set as 50% of the net income of farmers during last year, with basic pension and individual account taking half and half.

### *7. Setting a normal adjustment mechanism for basic old-age pension*

Setting a normal adjustment mechanism for basic old-age pension is an important measure to guarantee the basic living standards for the retirees and also an important manifestation for them to enjoy the fruits of economic and social development. International experience told us that the countries with the system all had a growth mechanism for the pension standard in relation with the change of prices and salary growth. China has for several times, adjusted the basic old age pension for the retirees since it had the system. But a scientific and standardized mechanism has not been built yet.

The basic thinking for setting a sound mechanism is to improve the old-age pension adjustment mechanism for company employees, and based on that, to gradually build a sound one covering government, public organization, and company employees. The adjustment of basic old-age pension should be based on price fluctuation and growth of workers' salaries and the adjustment range should consider the salary growth rate and price index and the basic old-age insurance fund and the capacity of the fiscal support. To curb the situation that people stop to pay premium after a full 15 years, and try every possible way to retire in advance, we should continue the principle of paying more, getting insured more, and while adjusting basic pension, we should emphasize on premium duration and level. We should also reduce the range of quota for universal adjustment and increase the treatment for those who retired later. And in principle, we will not lean our policy on the group with special identity. Meanwhile, the country should also adjust the minimum standard of the basic pension for rural and urban residents according to the economic development and price fluctuation.

#### *8. Postponing retirement age in a gradual manner*

Retirement age is an important factor affecting the old-age insurance system. The present practice that the male workers retired at 60, female leaders 55 and female workers 50, started since the 1950s. On the one hand, the retirement age is low and there are also some policies for retirement in advance. The actual age for getting pension was only 54, while the life expectancy for urban population already reached 78 and is becoming longer. On the other hand, the different retirement age for female workers and leaders resulted in conflicts in reality. At present, the threshold age for urban and rural residents to get pension has been the same, which is from 60. That for the individually insured was 55. As the economy and society develops and the average life span extends and people are receiving longer education, it is an inevitable trend to postpone retirement age. We should do it properly on considering the factors such as demand and supply of labour, education level, and life expectancy and fund balance. It could be done in two steps by starting from extending the retirement age for woman first and then for man. Firstly, we could adjust the retirement age for female workers from 50 to 55. Secondly, extending that for male and female workers simultaneously, from 55 to 60 and from 60 to 65 respectively. It is advised to release the plan during the 13th five-year plan period to solicit people's voice. And after amending and improvement, the plan is to put into practice during the 14th five-year plan period. We should give people an about 3-years preparatory period to arrange their career and life after retirement. Meanwhile, we should study and improve some supported policies on the retirement for those who did heavy manual work. We should cancel the policy on advanced retirement because of illness. For those who lost their working ability, we could give them allowance according to related regulations and let them retire when they meet the age requirement. For those individually insured people, we should also adjust their retirement age in a timely manner and improve the policy to promote their employment and encourage employers to create posts suitable for old-aged people and guide them to work or start their own businesses.

#### *9. Promote fund investment to preserve and increase its value*

As the social insurance develops, the balance of old-age insurance fund increases rapidly. With the acceleration of urbanization, more and more will take part in the old-age insurance program in the future, so the fund will also increase and it is expected to reach an accumulation of nearly a trillion Yuan in the coming 10 years. Months ago, the Ministry of Human Resources and Social Security and the Ministry of Finance sought people's advice on the Regulation on Investment and Management of the Basic Old-age Insurance Fund. That means the balance fund will go to market for investment. The regulation stipulates the channels for fund investment and its capital quota. It should be put into practice as soon as possible

after soliciting opinions. The old-age insurance fund in the world, whether it is full accumulation system or pay-as-you-go system, all take a strategy of diversified investment to preserve or increase its value. Some conservative investors, such as Singapore's central public reserve fund, began to gradually change their style. The fund account was only allowed to buy special state bonds before, but now it could go for market investment. Meanwhile, those fund, which was only used for market investment previously, such as the individual account of Chile, the DB, DC fund of the US, Canada's pension planning, and California's government employee retirement fund, all expand the quota of equity asset and are trying other investment channels. The fund from some countries also tried going global for investment. All these show that against the backdrop of ageing society, slowdown of economic development in many developed countries and the economic globalization, all countries actively use the force of market and seek more returns by diversified investment to reserve and increase the value of their old-age insurance fund, relieve budget burden and improve its replacement level. However, practice proves that the marketed and diversified investment for the old-age insurance fund is not accomplished at one stroke. It all started by investing on fixed income products, and then as the capital market developed and improved, and the managing organization improved their ability to steer the capital market, they began to increase the quota of equity assets. The regulation on investment of China's old age insurance fund, told us it takes time for related policies and management to improve, for the coordination and cooperation among decision-making, executing and supervising bodies, for the shaping and improvement of multilayer capital market and for the investment organizations to improve their ability to cope with changing financial market. So all these determine that the marketed and diversified investment should be done in a gradual way. In light of the special nature of old-age insurance fund, safety and appropriate mobility are more important than its profits. At present, China's capital market indeed has the drawback like lack of financial products, unstandardized operation of listed companies and lack of a multi-layer and multi-structural market. Therefore, we advise to combine fund investment with regional economic development. Only the fund promotes social and economic development, can it be share the fruits of economic development and accumulate real and tangible purchasing power. On this, the international practice has given us rich experience. Singapore's central public reserved fund was invested in infrastructure building, the huge house leasing program in particular to let everyone has a house to leave. The country's employees' reserved fund, after privatization, was used to support private economy. It promoted the infrastructure building such as power station, airport, highways and port by buying non-public bonds and direct loans, stimulating economic development as a result. The California's government retirement fund also put local investment a priority, and is always an important part of local economic system. All these show that the purpose of old-age insurance fund is not only for the increase on the accounting, but also for promoting the regional economic development. The latter is the root for preserving and increasing the value for the fund. China's capital market needs further improvement and standardization. This condition determines that the present investment focus for China's old-age insurance fund is to support real economy. On the one hand, it could be used to support infrastructure building through loans, purchasing state bonds or bonds issued by local government. It could be in particular used to support affordable house building program. On the other hand, we could increase its investment in private equity to help the development of small and medium companies with huge potential (like high-tech and bio-tech companies) to achieve a high return.

Risk accompanies investment. Therefore, we need a series of supporting measures and policies. One is to set up a system and mechanism to guard against risks. One of the important measures is to set up a system on investment evaluation and grading, information releasing and a mechanism on exit and access. On evaluation and grading system, emphasis should be put on evaluating and grading different

investment products and the operation organizations. We advise to put the old-age insurance fund operation on the agenda of each year's Two-Sessions (National People's Congress and Chinese People's Political Consultative Conference) and release related information to the public. It is money for people's future use, so people's right to participate, to know and to supervise should be given a full play. Second is to improve legal system for pension fund investment and management. The State Council should step a management system for old-age pension fund to clarify related contents, regulate on related departments and behaviour of the investment organizations. Third is to set up a supervision system for fund investment. We advise the Ministry of Human Resources and Social Security to set up an Investment and Supervision Bureau for Old-age Pension Fund. Their task is to supervise the investment of pension fund, enterprise annuity, occupational annuity and national social security fund. The role of social supervision and supervision by other departments should be played out. Fourth is to clarify pension fund collection and distribution of investment returns. Fifth is to improve investment risk prevention and control mechanism. We should strictly limit investment scope and ratio. The fund should not be managed together with other types of capital. The investment organization should draw some money out of their management fee to compensate possible losses. Related organizations should set up system for internal control to earnestly step up risk management.

*10. Fully implement the old-age insurance reform of government organizations and public institutions*

The specific policies on reforming old-age insurance of the public and government organizations have been clarified and will be put into practice in 2015. The difficulties are as follows: First, how to guarantee a smooth transition for the middle-people (who work before reform and will retire after reform) in these organizations under current policy while ensuring their treatment not affected. Second, how to ensure the pension for those people who worked at public organizations but were not on their official payroll. Most of them are to retire soon. They cannot take part in old-age insurance scheme for public organizations and have not been in workers' insurance scheme. Third, some public institutions are not fully reformed. They may face difficulties to pay premium, as the premium rate for them is 20% and individual, 8% and a further compulsory occupational annuity. We suggest related departments to carry out specific measures to solve these difficulties.

*11. Set up a system of treatment for family members of the deceased and allowance for the sick and disabled*

We should set up a system for treatment for family members of the deceased who got insured and allowance for the sick and disabled because of illness, to form an integrated security network.

i. Standardize the treatment policy for family members of the deceased

At present, the treatment for the family members of the deceased in government, public institutions and companies is with a huge gap and through different channel of payment. The basic thinking: First is to clarify the function of the system to alleviate the economic burden of the family of the deceased to arrange funeral and give certain but not too high material support for the family. Second is to clarify the items and payment ways for the treatment for family of the deceased, which should include funeral assistance and pension for the family and be paid one-off. Third is to standardize the payment channel. The treatment should be paid by the basic old-age insurance fund.

ii. Set allowance system for the sick and disabled

According to present policies and regulations, workers could enjoy retirement treatment when they lost working ability because of sickness or disability. The social insurance law regulates that we should set up a unified and standardized system which links with old-age insurance system. The basic thinking: First is to aim at establish a separate and integrated illness and disability allowance and combine the policy of retiring from post and retiring because of illness into it. Second is to abide by the principle of enjoying allowance on the condition that they paid premium. We also should avoid the moral risk of getting insured after illness and differ the system from social relief and aid. Third is to reasonably set standard for treatment. On the one hand, we should consider the national condition and bearing capability of the fund to ensure people's basic living. On the other, we should connect the new system with the old and ensure they could enjoy regular pension after reaching their retirement age.

#### *12. Extending minimum duration for premium*

Judging from one person's life cycle, the period before age 24 is generally education stage and working stage between 25 and 60 and old-age life stage between 60 and 80. People should keep paying premium during the average 35 years of working period to accumulate rights and interest for old-age insurance after retirement. Considering factors that people may suspend work, the minimum duration for premium should be no less than 25 years. However, in 2012, the average duration was only 24 years (among it, average actual premium duration was 10 years and duration regarded as paying premium was 14 years). The advanced retirement ratio was 9% and suspending premium ratio was 15%. All these severely affected the balance of the fund and resulted in low pension for some of the retirees (especially the females). We advise to extend the minimum duration to 25 years. To keep a continuity of the policy, for the people who reach retirement age, but not pay premium for less than 25 years, we should extend their premium to full 25 years. We should consider adjusting the duration while amending social insurance law.

#### *13. Vigorously develop company's occupational annuity to improve the multilayer system*

Chinese workers' multi-layered old-age insurance system is composed of basic old-age insurance, enterprise annuity or occupational annuity and old-age insurance with personal savings nature. At present, the enterprise annuity develops slowly and covers less people, as there is only 6% of people take part in the program. Individual savings old-age insurance has not built yet and most of retirees rely on basic pension. The way for social security is simple and the government bears a heavy burden. The main problem affecting the development of supplementary old-age insurance is lack of policy support and guidance and it needs to be improved. One is to accelerate expanding coverage of enterprise (occupational) annuity. We could properly lower the premium rates for companies and institutions by reforming and improving basic old-age insurance system to leave room for developing enterprise annuity. Second is to practice EET model for tax policy. In reference of international practice, we could further adjust the tax policy on enterprise and occupational annuity. Meanwhile, should study policies on tax support for individual savings old-age insurance. Third is to develop enterprise annuity pooling plan. Big enterprises, due to large number of employees and huge amount of capital, can design their own investment plan. But for SMEs and social organizations, it is difficult to do so because of small scale of money and high operation cost. Therefore, we should encourage them to pool their annuity together to reduce management cost and improve operational efficiency. Fourth is to integrate insurance system between different levels. We should do a good job in integrate basic old-age insurance with rural and urban subsistence allowances and related social welfare and relief and aid policies. We should continue to play the role of land security and family security. At present, the personal savings of Chinese residents

have reached over 40 trillion Yuan and commercial life insurance also developed to a level. People with high income are encouraged to take part in commercial insurance to improve the life quality after retirement.

#### *14. Improve social security fund supervision and management*

##### *i. Improve laws and regulations on social security fund supervision*

We should promulgate an integrated regulation on fund supervision law enforcement and fraud handling. Meanwhile, we should enforce it strictly to hold those who violates responsible.

##### *ii. Build a professional team for supervision organizations*

The central, provincial and municipal government should exercise the rights of supervision and the top level should set sub-organizations to lower level to form a separate supervision system.

##### *iii. Create a system for prevention, investigation punishment, and evaluation*

We should standardize decision-making, management process and improve internal control to prevent and control risks from the root. We should improve fund supervision information system to step up real-time supervision on fund collection, payment and management. We should step up law enforcement on fund supervision to punish those who violate laws and regulations such as embezzlement, fraud. We should implement the criminal law explanation by the CPC standing committee and step up coordination between police, and judicial departments to improve efficiency of punishing violations. We should also build fund safety evaluation and analysis system and achieve a quantitative analysis on fund risk to improve the accuracy of supervision. We should also release the punishment cases to the public to expand the right to know of the public and serve as warning education.

##### *iv. Improve the all-round supervision system combing administrative organs, CPC and society*

We should actively play the role of the labour union, various organizations, public, media and social organs in supervision. We should ensure general public to exercise their right of supervision by improving decision-making rule and process, information releasing, public reporting and awarding system. We should improve mechanism on reporting and handling of the problems and integrate administrative and social supervision. All these is for the setting up of an all-round supervision system to secure the fund and improve people's livelihood.

#### *15. Improving management and service system*

##### *i. Further integrate management and service resources*

We should make it clear that the power to the management organization is to practice these functions well like executing policy, managing fund, and providing service. We should set up social security management and service bureau under Ministry of Human Resources and Social Security and the similar organs at provincial and municipal level and branch at country level. We should integrate the organizations handling workers basic old-age insurance, government and public institution employees' old-age insurance and new rural insurance (urban and rural residents insurance) to improve operation and service network and grassroots public service platform.

##### *ii. Optimize operation model and service means*

We should promote online operation of social insurance, expand public service channel and explore outsourcing services. We should accelerate computerization of social security to foster E-social security by relying on information technology and network coverage, implement accurate management by pooling and effective use of data, and achieve all be done on one integrated social security card.

iii. Improve grassroots public service platform

We should integrate all network and service resources of the grassroots service organizations and social service organizations to build a employment and social security service platform at all sub-district and township levels and set up employment and social security station at all community and villages. We should set up a coordinator system at all villages. All is to improve service network for grassroots social security business with city (county) as core, sub district (township) and community (villages) as basis.

iv. Improve computerizing social security services

One is to fully use social security card. We should build a basic information data for social security cardholder, as the people will reach 1.2 billion at the end of 13th five-year plan and cover 90% of population. And we should reach the goal that the card can be used with multi-functions and across the country. Second is to pool social security information together and promote data sharing and business coordination. We should accelerate integration of management system with achieves system and improve digitalization and visualization of achieves to pave the way for achieves resource sharing across the country. We should build a unified information exchange and business coordination platform by improving cross-regional business handling. We should promote cross business, cross-region, cross-level and cross-department information sharing and business coordination to form a unified platform. Third is to use big data and cloud computing technology in social insurance area. And we should explore supervision, information analysis and decision-making based on big data. We should continue to expand network monitoring. We should improve network supervision system, data collection, trimming and cleaning mechanism to improve data quality and analysis. We should improve business-monitoring model, fund supervision system and medical behaviour monitoring system to explore computerized monitoring, gradually expand business application scope and improve decision-making support. Based on data storage technology, we should further improve decision-making support system, carry out theme analysis, data demonstration and warning and prediction and explore building of analysis model, to build an information-based statistics and surveying platform.

## Topic 1.1.1 (Initial)

Social Insurance Administration Service System<sup>2</sup>

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<sup>2</sup> Excerpt from report by Chinese expert Mr. Tan Zhonghe



## 1. Integrate resources and realize unified management of social security

The management system relates to the interests of government agencies, the stability of social security teams, as well as the vital interest of the public. Practical measures should be taken to gradually integrate the services, and the rush for success should be guarded against.

First, we should finish the integration of the old-age insurance and medical insurance for rural and urban residents as soon as possible. The State Council has made it clear to combine the old-age insurance for urban residents and New Rural Old-Age Insurance into one basic pension scheme that will be managed in a unified way. Public health and family planning agencies should transfer the New Rural Old-Age Insurance to human resource and social security agencies, and build an integrated medical insurance program for unified management, according to the State Council's plan of institution reform and function transformation.

Second, we should integrate the management system of collecting contributions, transfer the payment at local taxation authorities to commercial bank outlets under the management of social security authorities. According to the fund-collecting procedure in China, social security department will be responsible for registration, reporting payment and checking the base. When the evaluation is done, banks will collect the fund, deposit it into separate accounts (consolidating fund account and individual transaction fund account), and then transfer to a special account for social insurance fund.

Currently, commercial bank network for collecting contributions have covered rural and urban areas. It is unnecessary that tax authorities add the fund management and extend the management chain. Besides, tax authorities only collect contribution paid by regular employers. It is social security agencies that collect the contribution of most medium-, small and micro-sized businesses, individually-owned businesses and flexible workers. Tax authorities only collect old-age insurance and medical insurance contributions. As the number of flexible workers, individual insures increases and the Social Security Law demands the combination of five insurances into one, the practice that tax authorities collect contribution can no longer satisfy the development of social security. Regulations should be introduced as soon as possible to transfer the collection duty from tax authorities to social security institutions for unified management, and designate commercial banks to collect the fund.

Third, we should integrate all intermediary service providers set up by all levels of human resource and social security departments into Social Security Bureau for coordinated management of basic old-age insurance, unemployment insurance, medical insurance, work-related injury insurance and maternity insurance. Intermediary service institutions above prefecture level manage and supervise social security affairs. We should gradually abolish the service of specific affairs, which should be undertaken by the public service platform and public institutions (commercial institutions) of the counties, cities, regions and village communities. Now that human resource and social security departments at prefecture and city level no longer design social security policies, they should be integrated into the Social Security Bureau.

Fourth, we should integrate social security programs including old-age entitlement, award and subsidy of family planning and the old-age care for village cadres, change multiple management and eliminate redundant investment. Specific measures includes transferring the old-age entitlement under civil administration to human resource and social security departments, and incorporating it into the old-age care of the rural and urban residents; incorporating the old-age subsidy for veteran village cadres and party members under the civil administration to the old-age care of the rural and urban residents; transferring the subsidy for family planning to human resource and social security departments, the old-age care to the unified management of intermediary service institutions. Meanwhile, we should sort out subsidies for targeted groups, and these subsidies include social special care, the old-age subsidy for people on the confiscated land, pension for the disabled or for the family of the deceased, subsidy to the family of workers

deceased because of non-worked-related reasons, subsidy to the spouse of the retired, so that these programs will be managed in a unified way.

Fourth, we should create conditions to integrate all social security affairs of other departments (such social insurance, social relief and social welfare) into same-level Social Security Bureau, and elevate these bureaus to be directly under the government. The Central Social Security Bureau is directly under the State Council, so it is a ministerial-level agency. Provincial and county-level Social Security Bureau is directly under the provincial and county government. Our goal is to complete the reform at all levels by the year 2030.

## **2. Classified management of staff at intermediary service institutions**

According to China's conditions, all institutions should be of administrative nature in the short term (around 10 years). Classified management of staff will be practiced. Positions within each intermediary service institutions will fall into three groups: administrative, professional and operational. Administrative staff will be incorporated into the management of civil servants, professional staff should be incorporated into the management of technical staff of public institutions, and operational staff should be incorporated into the management of social workers and managed with qualification authentication. In principle, labour contract management will be combined with socialized administration. Management staff accounts for 10%, professional staff account for 30%. Other operational positions can be assigned by other institutions or qualified agencies with bidding competition, regular evaluation and professional management.

Basic principle for determining the operational position should be to consider the factors influencing the staff at intermediary service institutions, and these factors should mainly be the workload that cannot be simply determined by the ratio of staff to consumers. Factors to be considered are as follows. First, the level of economic development of one region. A region with high economic growth, larger population, more advanced transportation and communication has better-quality population, so such regions have more service-receivers. Second, distinguishing downtown area, suburbs and rural areas. This has to do with the public service resources. Population and public service facilities and resources are concentrated in downtown areas, so other things being equal, there should be more service-receivers. In comparison, public service resources are less in suburbs and rural areas. These factors must be taken into account when determining the per capita amount of service. Third, the per capita amount of service should be calculated based on the handling of old-age insurance and medical insurance (including work-related insurance and maternity insurance). As two importance insurances, they are very different in daily operation and compensation payment, though they are similar in insurance purchase and contribution payment. If they are treated in the same way during institution size determination, their differences will be concealed, leading to uneven distribution of workload and resource waste.

## **3. Take the opportunity of insurance for all and consolidate the foundation of management service**

"Registration of insurance for all" is important for the long-term and sustainable development of social insurance system, achieving the fairness in social security and consolidating the foundation of social insurance management. Registration of insurance for all will improve the database of the insured employees by building a database and registering legal persons; establish a database for insured urban and rural residents through the registration at community service centre; establish a database for the insured students through school's record; realize the comparison and exchange of information with public security's database of household registration. Registration of insurance for all consolidates the basis for social security management, and we should take this opportunity to strengthen basic work. First, guided by the demand of the insured for management service, we should promote unified, ICT-based, and standardized service, accelerate issuing standards, launch online service and issue social security card to make sure all insured has a card and promote its use. Second, we should strengthen the service team by classified management, improved position arrangement, strict discipline and

promote work ethics focus on civilized services, so as to deliver careful, dedicated and considerate services. Third, we should optimize the intermediary service model. Models should be transformed from being opened to a specific group to the urban and rural resident, from tax collector system to an integrated tank system, from lobby service to a combination of lobby service and online service, from service network stations concentrating in urban areas to roads, communities, and rural labour platform, from unified management by the intermediary service institutions to the purchase of public services through multiple channels. In this way, we can improve the accessibility of intermediary services.

#### **4. Explore the corporate governance structure of social insurance**

According to public management theory in the west, the increasing demand for public service requires the government to reform its philosophy, functions and organizational institution, break the existing bureaucracy, and instead build a management system guided by the public need and a service philosophy. New public management theory believes the relationship between the government and citizens is a subject-object relationship with a customer orientation. The social contract theory believes public service institutions belong to the government agencies, and their administrative nature and lack of independence is the source of poor service capacity. The commanding and controlling practice in some places should give way to communicative, consultative and administering model. Public service institutions with capacity to integrate and quickly respond should be built.

At the initial stage of social insurance, it is necessary for intermediary service institutions to rely on administrative measures. However, with universal coverage, the conflicts between demand and supply of such institutions becomes sharper. It is especially true that when China is building a service-oriented and law-based government, administrative measures alone cannot satisfy the public demand for social insurance, and governance mechanism and service manner of public service must be introduced. In terms of the institution, the service model relying solely on government agencies should be changed into a market mechanism for privately operated services and a governance mechanism with public participation. In terms of the organizational system, we should build a flat system. To put in place a corporate governance system, we should follow the internal laws governing the social insurance management, and explore different programs to encourage qualified public organization to participate, and gradually give the market the decisive role in allocating resources. Then we should identify what services can be provided by intermediary service institutions themselves, what can be outsource, what can be provided through the market. In this way, we can make better use of social resources, improve efficiency and capacity, and prevent disorderly expansion of intermediary service institutions. Some features of social insurance decide that some operational positions can be outsourced. Partial outsourcing, social governance and public participation can offer the insured more choices. This is similar to commercial banks and insurance companies where people can choose a service station as they wish. Only through following the new theory on public governance and public participation can we address the lack of fund and staff as well as improve service quality and level.

The key to the corporate governance structure lies in speeding up the reform of public institutions and social organizations, as they are the major provider of public services. Currently, all intermediary institutions are under the government, they are the supervisors and the service providers. According to corporate structure, gradual reform should be carried out. Following issues should be studied. First, the independent legal person status of intermediary service institutions should be identified through legislation. The goal is that they can independently assume civil legal liabilities. We should accelerate building an independent property system of legal persons, so that they can truly become independent legal persons of institution and major public service providers. Second, we should abolish the administrative nature of the intermediary service institutions when conditions allow, so as to transform them into legal persons in real sense. Third, we should speed up the legislation process and determine the legal process for the quality granting and alteration. Finally, we should accelerate policy and institutional design for letting the public decide the

allocation of public security resource, so as to create a level-playing field for public institutions, social organizations and commercial institutions.

### **5. Centre on the ICT application and address understaff with technology**

Understaff of intermediary service institutions should be solved by hiring more staff or relying on computers and information technology to improve the efficiency and lower labour costs. The latter is obviously more practical. That's why we should focus on spreading application to deliver more efficient and convenient services. If more than 90% serviced can be delivered through the Internet, text messages, WeChat, Weibo and self-help machines, much human cost can be saved, and understaff can be addressed through high technology. Therefore, we must integrate all sorts of applications based on social security cards and e-cards, and speed up online social security. Currently, we should build standards for card application and online social security. An insurance registration system, a national service system of online inquiry of individual record, a system of hospital settlement and old-age fund management outside of one's hometown should be established. By this means, we can put in place a four-dimensional system, namely an information-sharing platform, a management and service platform for floating population and people who live and go to hospitals not in their hometown, a real-time monitoring platform and an education and training platform for the management staff. We can thereby supervise the intermediary service institution, so that they can more efficiently manage the fund and safeguard the rights and interests of the insured.

### **6. Speed up designing and implementing standardized social security management and realize precise management**

First, we should accelerate designing and implementing the standards for social security management. Standardization is necessary for improving management capacity and the basis for realizing precise management. Three national standards including the General Principles for Social Insurance Services, and three industry standards including the Visual Identity System of Social Security have been issued. We should take these documents as an opportunity to speed up standardizing social security management. Second, we should gradually setting up a monitoring, predicting and warning system, apply scientific method to the management of social security. We value quality management and quantity control. We will replace ambiguous and vague requirements with specific quantified standards, models and calculations, and extend quantified management to every link of the management service. Quantified data is the basis for raising questions, making judgments and evaluation, so as to guide, adjust and control the behaviours of the insured. Then analysis into current and future expenditure, income and certain risks of the expenditure and income will be conducted before putting forward precautionary measures. Third, the top-level management of social insurance should be transformed into matrix and grid management. The information transfer of top-level management is one-way, while matrix and grid management can connect and coordinate dots. The latter can provide service to the insured on any dot within certain scope, and this can solve the fundamental problem of transferring and renewing social insurance relations. Fourth, on the basis of ICT application and the Internet, we should introduce big data, cloud computing and the Internet of Things to the intermediary service of social insurance. Management and services, such as intelligent identification, positioning and monitoring can be realized step-by-step, so that people and people (through PC and non-PC), people and things, things and things can interact with each other, and the Internet of Things will be applied to social insurance management. The intelligent information provided after the interaction can greatly improve the capacity and level of intermediary services.

### **7. Establish a security mechanism of fiscal fund management**

First, the calculating method of fiscal budget to social security institutions is different from that to other government agencies, i.e. according to capitation. The method is dictated by the internal

demand of the intermediary service. The Social Security Law makes it clear that the government is responsible for the management fees of social insurance, and the central government helps poor regions through transfer payment. The fees can also come from the contributions through legislation. At present, the most pressing issue is to increase the fees. The fees should be 2% of the annual contributions according to international experience and estimates.

## **8. Four-dimensional management service platform**

The era of cloud computing and big data is with us, we have to follow the trend and build a four-dimensional management service platform.

### *(i) An information-sharing platform*

The platform can achieve three purposes. First, government agencies, such as the tax authority, industrial and commercial administration, police security, civil administration, public health department, designated medical institutions and drug stores, can maintain real-time exchange of information with the central database of social insurance. Second, information of the insured can be shared across regions promptly. Third, the data of intermediary service institutions can be shared in a timely manner.

### *(ii) A management and service platform for floating population and people who live and go to hospitals not in their hometown*

The focus will be on medical care and old-age care outside of one's hometown. The platform consists of three functions. First, it allows the real-time viewing and exchange of information on the insured and policies, and the comparison of the parameter information of social security policies among different regions. Second, it automatically evaluates the reasonability of treatment. Third, it collects the information of medical treatment and old age care provided outside of the recipient's hometown, and can complete the qualification authentication.

### *(iii) A real-time monitoring platform*

The platform collects information on the operation and financing of the employers, on the employment and income of the employees, on the livelihood of pension receivers, and on the medical service received by patients. Once unusual situations are discovered through off-site data collection and monitoring, on-site inspection can be in place as soon as possible. Meanwhile, a blacklist will be drawn up to include employers, employees and medical institutions that conceal information or that dodge, underpay, evade, and deceive payment. Those listed will be top targets for supervision.

### *(iv) An education and training platform for management staff*

The key to improve the service capacity lies in a highly-skilled team, making a long-term training mechanism necessary. Real-time training can be realized through online distance education and an information-sharing platform, which is affordable, advanced and flexible. The platform consists of following parts. First, a central database. A database of service data will be built for distance viewing and searching. Second, distance courseware. Skilled teachers will be hired, and video courses will be made available to learners. Third, an automatic evaluation system. Participants can examine how well they have mastered the knowledge through online tests. Last, a certificate system. Those who can meet the requirements though learning and examination will be granted a certificate, which can be regarded as a reference for employment and promotion in management service of social security.

## **9. Study on Social Insurance Administration Programs and Projects with the Involvement of Social Organizations and Commercial Institutions**

First of all, we shall propose a project list of social insurance services that are open to social organizations and commercial institutions in order to provide regulation and policy references to these entities. Second of all, we have to include public services covered by social security into government procurement, design a detailed implementation plan for government procured service programs, and develop open and transparent procurement processes for social insurance services; in principle, any regular social insurance service must be procured based in principle on a mechanism of competition and by contracting with or entrusting another social organization. Third of all, we have to build a law-based service supervision system for social insurance administration to guarantee the social security rights of the people and to ensure equal and fair competitions among all kinds of service providers. Hence with the supervision system, we shall clearly define the scope, within which social security providers participate, and identify regulation processes and build an effective system composed of administrative, professional and market regulation over various operations including bid-invitation and tendering, inquiry, and entrusting. We have witnessed some enlightening pilot projects on service procurement in some regions: rural social insurance services at grass-root level has been procured by county/town governments in Hubei Province. Since the reform of social entities at county/town level in 2005, a new administration mechanism called “sponsoring social entities” has been established. The mechanism is led by governments, financially guaranteed, market-oriented, and is based on fair competition, managed according to contracts and supervised by the public. Besides, some services including social security has been outsourced to nongovernmental organizations. In Chongqing, the government has been using a network of commercial insurance institutions covering both urban and rural areas for providing rural social security. After several years of attempt, they have succeeded in offering rural social security with commercial insurance institutions—a new path of multiple-layered administration system of rural social security. Since 2006, Jiangyin City in Jiangsu Province has been entrusting commercial insurance companies to managing new rural cooperative medical insurance services. All the above trials have laid a foundation for us to build a new legal-person administration structure for social insurance which is “led by the government, maintained by social organizations and supervised by the public”. Resting upon the experience of all regions and the institutional reform of social entities, we will gradually put this structure into practice.

## **10. Improving the Legal System supporting Social Insurance Administration**

There is no complete law or regulation on social insurance administration in China at present. Despite special chapters and sections in the Social Insurance Law designating rules for such services, these rules are only in the paper, not operable. Based on Regulations on Collection and Payment of Social Insurance Premiums, Administration Methods for Recordings of Individual Rights Covered by Social Insurance and the relevant administrative rules and regulations, we shall consider developing Regulations on Administering Social Insurance Services and confirm the rules on each link and process of administering social insurance, how to provide social security services, and the rights and responsibilities of people who enjoy social security services.

## **PROJECT RESULT 4**

### **National policy framework for a full coverage of old-age insurance system**

## Topic 1.3.1

Public Sector Pension Reform<sup>3</sup>

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<sup>3</sup> Excerpt from the report by Ms Zhang Yinghua



Target of GOPI (Government organs and public institutions) reform is to achieve justice, liquidity and financial sustainability. Justice embodies in unify treatment, corresponding rights with responsibilities, and narrowing gap between GOPI and Urban Enterprise Pension system; the liquidity reflects in the pension interests can be protected with labor mobility, without "portability loss"; Financial sustainability requires to guarantee certain level of replacement rate, balance of payments, or the deficit is controllable that can be made up without bring unbearable pressure on the government at all levels.

## **1 Strengthen the justice of system**

### *1.1 Set reasonable contribution base*

GOPI pension system is designed to achieve uniform with urban enterprises basic pension insurance, but the statistics contribution base are inconsistent .Pension contribution base is basically all labor income with higher degree of labor remuneration monetization , while GOPI have much higher proportion of implicit wage, most GOPI remain the reform subsidies (transportation allowance, communications allowance, housing allowance, education and medicaid, heating subsidies which covered by the previous system ), but contribution wages of GOPI do not include allowances and subsidies. From the perspective of the unit, it is advantageous that can reduce current contribution expenses, and postpone the financial burden; but from personal point of view, future pension will be affected by the reduced the contribution to personal accounts of basic pension insurance and account of occupational pension .

In view of this, we should improve the supervision mechanism, and establish pension supervision committee which consist of employees and retirees on behalf, principal of the relevant government departments, experts and scholars, to insure pension rights fully understood, and be able to supervise unit to contribute pension insurance in accordance with labor income agreements, to ensure individual right of knowing and future pension benefits.

### *1.2 Ensure the revenue and interests rights of the virtual bookkeeping part of the account*

Personal accounts of GOPI basic pension and unit contribution of occupational pension both use virtual bookkeeping way, but with slightly different: the basic pension of individual contributions to personal accounts, but the funds have been incorporated into the social pooling fund for the current payment for retirees. In fact , it is "financial transform "between the social pooling account and individual pension accounts.<sup>4</sup>Unit contribution to occupational pension accruals accounts implement virtual bookkeeping without actual capital until retirement , in fact, it postpone the unit payment time from each month of working time to retirement .It is general practice to reduce the current financial burden.

The biggest drawback of "Virtual bookkeeping" is the loss of investment income , and then will affect the participants' future retirement income. "Decision of the State Council on the reform of GOPI pension system" and "Government Organs and Public Institutions Pension Rules", stipulate that personal accounts of GOPI basic pension and unit contribution of occupational pension should calculate interests annually in accordance with the national unity bookkeeping interests rate, but do not clearly defined how to determine the accounting interest rate.

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<sup>4</sup> Hu Xiaoyi, vice minister of human society on the GOPI pension system reform answer,

[http://www.mohrss.gov.cn/SYrlzyhshbzb/zwgk/SYzhengcejiedu/201501/t20150119\\_149495.htm](http://www.mohrss.gov.cn/SYrlzyhshbzb/zwgk/SYzhengcejiedu/201501/t20150119_149495.htm)

To avoid loss of pension benefits, we should define the accounting interests rate equal or close to the market investment interest rate. Further, in order to protect the safety of the fund account, we also need to determine a security rate.

## **2 Strengthen liquidity of pension system**

According to "Decision of the State Council on the Reform of Government Organs and Public Institutions Pension System", if the insured leaves the original unit, and continues to insure in the new unit, the pension payment period can be accumulated; transfer of pension relationship divided into two situations: First, flows between organizations and institutions within the same range of contribution, only transfer pension relationship, without funds; second, the overall range of flow between different GOPI or enterprises, both transfer pension relationship and fund, with all fund in personal accounts of the basic pension insurance and 12% of the social pooling fund according to actual wages for each year to transfer. This shift measure is consistent with the existing connection measure of basic pension insurance for urban enterprise, but according the actual operation of basic pension insurance across region transfer. Resistance of pension fund transfer is not completely eliminated, due to local protectionism and subject opposed of vested interests, local government do not want to transfer the funds especially region in loss.

### *2.1 Pension insurance relationship transfer between different contribution regions*

In the short term, GOPI pension insurance cannot realize national co-ordination, different financial sources of funds result in fragmentation daily operation, investment management, the gap between the contribution scale and benefits level. In the labor mobility process, if treatment fall, personal against; if treatment uplift, the receiver oppose. Currently policy stipulate that labor mobilize among different contribution region, leave the 8% personal actual contribution of wages in the original place, for the outflow of labor, this is a kind of compensation for the loss of human capital, but for labor inflows speaking, it is a loss of the pension system, because inflow region accept all the contribution years, but received only partial payment, equals with 12% contribution rate, to some extent, increase the financial burden of the inflow.

French pension system is managed by various agencies; transfer of pension insurance relationship is through consultation between agencies. According to the agreement, transfer mechanisms can compute contribution years segments and pay pensions respectively, if pensioners meet retirement condition; if employees do not meet retirement conditions, relationship of pension insurance and all contributions can be transferred to the receiver agency, while meeting retirement condition pension paid by the last receiving agency.

Implications for China: only all contribution from units and individuals transfer to the receiving agencies so that pension will not be an obstacle to labor mobility. Therefore, when public sector pension relationship transfers among different contribution region, in addition to the amount of personal savings accounts, pension should be fully transferred to the labor inflow, in accordance with the actual contribution rate during the work time.

### *2.2 The pension relationship transfer between public sector and private sector*

When the GOPI staff departure and employed by enterprise, the transfer issue in addition to the basic pension insurance relationship and funds, but also involves the transfer of occupational pension accounts. For the basic pension relationship between the transfers, agencies can refer to existed methods, but it is more complex for the transfer of occupational pension accounts:

First, the GOPI occupational pension take virtual bookkeeping way, but established enterprise annuity take account operation, two operating mode cannot be directly transferred.

Second, if the enterprise does not establish enterprise annuity plans, in accordance with established practice, occupational pension account will remain in the original unit, which result in occupational pension account holders lose the accounts domination rights and the account fund investment supervision. Over time, some of the accounts may become bad debts.

Therefore, before complete the successful transfer of enterprise annuity with occupational pension accounts, fiscal need to save money to occupational pension accounts. For the enrolled enterprises which do not establish enterprise annuity plan, we need establish a transitional mechanism for the fund under the supervision of an independent government agency, occupational pension funds should be fully transferred from the original unit when departure happens , but in order to avoid personal extraction and discretionary before retirement, so that fund should be transferred to a designated account . Trustee take unified management and execution functions until the funds to be transferred to the enterprises to establish enterprise annuity, and then incorporated the occupational pension fund to annuity account.

### **3 Strengthen the financial sustainability of system**

After the GOPI pension reform, calculation and contribution base change from the last month's wages to career wage indexation, so that narrowed contribution base reduce the financial expenses of GOPI pension system. This is in line with the international trend of pension system reform in the public sector, and also to ensure the unify with Urban Enterprise Pension system. However, due to the serious old aging problem, the GOPI pension system still exists financial sustainability problem . So, the following recommendations:

#### *3.1 Taking long-term actuarial technology, use reasonable system parameters*

Sweden and Poland and other countries to implement the NDC account, combine the advantages of the payment type (DC) and the PAYG system together. because the system is too complicated, result in few followers , but it is still a great reference.

Similarly with the NDC account , China's GOPI pension system also has virtual billing design, the current accounting year deposit interest rate is still the interest rate. If we get experience from the NDC account of Poland as reference , that is taking the factors of economic growth and demographic changes into the account of the accounting rate in this way can the use of actuarial techniques to help determine reasonable and appropriate methods of calculation and payment rates, thus contribute to long-term financial sustainability of system. There are several important parameters in the GOPI pension system: contribution rates, the number of months calculated by individual account pension, accounting and pension growth rates. Parameters of system will have a significant impact on financial sustainability .

**Contribution rate.** The decisive factor of system revenue collection. From the view of operation of the basic pension insurance system for urban enterprise, because the maintenance burden vary widely, regions with heavy maintenance burden pension bear over 30 percent contribution rate , regions with lighten burden that pension contribution rate is less than 10%. It is foreseeable that this problem in the implementation of the GOPI pension insurance system will also appear. Obviously, this problem, indicating that the contribution rate design is unreasonable, without sufficiently thinking of the differences over the maintenance burden.

Recommendation: a floating rate should be considered, on the basis of the reference rates fluctuated, so the local government can select the appropriate contribution rate based on the actual situation and long-term revenue projections.

**Pension divisor.** Under the current regime, the number of personal accounts of payment months of basic pension insurance are fixed, such as 60-years-old count the number of months is 139. This means that for people retired at 60-years-old, the amount of personal savings accounts can only be distributed to 71.6 years, thereafter it will be a long-term risk system that individual account pension needs full financial commitment.

Recommendation: consider using dynamic counting of months, as the Swedish and German pension reform have done, considering changes in demographic trends, the wage growth and changes in market interest rates in the payment number of months.

**Accounting interest rate.** Accounting rates are the most critical factors of pension treatment. At present, accounting rates of the basic pension insurance for urban enterprise personal account is one-year deposit interest rate, it has long been lower than the inflation rate, leading to the real purchasing power of pensions personal accounts shrinking.

Recommendation: set guarantee interests, when the market interests of return lower than the guarantee interests, using the security interest; when the market interests is higher than the guarantee one, the investment interests of return in accordance with the actual market interests.

**Pension growth rate.** Pension growth rate can not less than the rate of inflation, otherwise it would be difficult to guarantee the basic life after retirement. Linking the pension with the price level, to ensure that pensions are not devalued; meanwhile, pensions should be linked to a certain percentage of wage growth, which would allow retirees to share the achievement of economic development.

### *3.2 Improve the earning capacity of the pension fund*

Reference on the Reform of the United Kingdom. UK public sector pension not only do not set an upper limit of contribution, but also set a higher contribution rate for high-income earners. China's GOPI pension insurance and basic pension insurance for urban enterprise has contribution up-limit, that the wage of three times higher than social average wage income is out of contribution base, which is the protection of high-income groups, in the short term, it may keep high-income groups in the social insurance system, to avoid adverse selection problems, but in the long run, it will reduce the pension income.

In terms of social equity or to enhance the ability of the Fund's income, we need to cancel the contribution up-limit, but considering the system the hardness of implement, we can consider raising the upper limit of the contribution base when needed, to put more income into high-income groups in base pay.

### *3.3 Expand the scope of co-ordination by the "big social co-ordination" to improve the financial sustainability*

The so-called "big social pooling" is to the pooling fund of GOPI pension insurance and urban basic pension insurance to the realize free transfer of all wage-earning class employees pension fund.

The reform stipulate that "GOPI pension insurance establish independent account, separately managed with enterprise employees basic pension insurance funds" ([2015] No. 2), it means that the GOPI pension contribution will form an independent pooling fund, not co-ordinate with urban enterprise basic

pension insurance fund. This arrangement may be considered a higher dependency ratio of GOPI. Coordinate use means that urban basic pension insurance fund may compensate to GOPI. To implement reforms smoothly, in view of the current public opinion trends, separated account management reform may be the path of least resistance, but it weakens the social insurance mutual aid capabilities at all levels, finance will continue to burden the GOPI pension, the aging population problem inside GOPI can not be diluted through population structure by the whole society, the financial endowment do not completely turn to social insurance.

As mentioned earlier, the Czech Republic, which is a country in transition, after restructuring its economy, the pension system in the public sector and private sector eliminate the difference in treatment between different groups, to achieve social justice, and labor mobility promoted.

Recommendation:GOPI and urban enterprise system have been unified on the basic pension insurance, should gradually unify system parameters and pooling fund, forming a basic pension plan that cover informal sector (to ensure contribution of employers) ,all employment, and secure universal retirees living.Reasonable gap can exist between pension plans in the public sector and the private sector , but this gap should not appear in the basic pension insurance. Differences of basic pension insurance contribution years only show individual wages (contribution level). Public and private sector pension benefits gap can be reflected in the occupational pension, the employer contribution rates of occupational pension reflect that necessary means of human resource management, the number of occupational pension employer contribution also reflect prices in different human capital in the labor market .

### *3.4 Encourage delayed retirement*

Recently, the Minister of Human Resources and Social Security announced in news conference, that postpone the statutory retirement age gradually from 2017. Delay the retirement age has been proposed for years, but has been unable to practice, mainly because of public opposition is relatively large. Under the current regime, the basic pension insurance for urban enterprise personal contribution rate is 8%, the individual total contribution rate of GOPI pension insurance and occupational pension is 12%, while each additional year of contribution, the pension replacement rate only one percentage increased. In other words, under this plan hair mechanism, deferred retirement is actually negative. Unless hidden job wages and bonuses accounts high ratio, 1 percentage does not have any incentive to delay retirement.

Contrast the different delay retirement policies of Germany, France and Austria .It can be found that the public only accept such policy that delay retirement benefits outweigh early retirement. German public sector personal pension without individual contributory , payment of the public sector in Austria borne entirely by the state finance, therefore, the two countries are taking incentive delay retirement mechanism that will significantly reduce the early retirement pension, retirement is significantly delayed increase pensions. Instead, the French local government civil servants required to pay pension premiums, increase the proportion of pensions does not motivate people to take the initiative to delay retirement, the government forced to increase the retirement age only through legal means.

Only when individuals do not bear contribution or contribution rate is relatively low,it is incentive to postpone retirement using that "delay retirement with the additional pension, early retirement reduce pension ," . Therefore, China's GOPI pension insurance can increase the minimum contribution years and the corresponding level of pensions, to inspire people to delay retirement.

## **4 Improve the performance of pension fund investment operations**

Operations experience of the basic pension insurance for urban enterprise show that due to personal accounts fund is in the social pooling accounts with social pooling funds for payment, The provinces of deficit expenditure can get central government subsidies, and provinces with profit surplus can form accumulation fund .From the national point of view, the total basic pension insurance fund accumulated surplus reached 3.5645 trillion Yuan.<sup>5</sup> Because GOPI pension insurance without national co-ordination, the central government will fund the same "deficit" of provinces subsidy, and the fund "surplus" province will accumulated surplus funds, we will face the operation problem of fund investment .

#### *4.1 Independence of trustees*

At present, the investment and operation of basic pension insurance for urban enterprise funds are based on National Council for Social Security Fund as the trustee, for example, Guangdong Province, commissioned 100 billion Yuan in March 2012 for NSSF investment operation, obtained 17.336 billion Yuan of investment income in 2014.<sup>6</sup> Shandong Province in February 2015 commissioned 100 billion Yuan pension fund for the NSSF investment operation. Since its inception in August 2000, the National Social Security Fund Council annual investment rate of return is 8.38%, while the inflation rate is 2.42 percent over the same period, to achieve better increasing the value of the fund. It should be said, the investment performance of the National Social Security Fund Council is quite good.

However, the National Social Security Fund Council belongs to the State Council institutions, whose assets are mainly from the central government budget allocations, the transfer of state-owned capital, investment income and personal accounts . Institutions and assets have close ties with the government, the independence of market institutions will be affected.

From perspective of institutions independence and decentralized of competition: choosing independent market institutions of the GOPI as trustee of the basic pension insurance fund.

#### *4.2 Trust management and investment performance evaluation*

The establishment of provincial government departments and institutions pension insurance council, entrusted all levels of government in the province, account records on behalf of managed funds and investment operations services; use trust management mechanism, improve the principal - agent mechanism, by choosing the appropriate market institutions investment operations, and establish a sound performance appraisal system occupational pension fund investment operations.

In recent years, from operator feedback of the situation of the enterprise annuity market , the biggest problem is the investment appraisal cycle is too short. Annuity performance generally for one-year short-term assessment period, for the three-year long-term assessment period, and to take the bottom out of the way, forcing the investment manager of corporate pension assets portfolio change hands frequently, greatly improving the management costs.

Recommendation: establish a long-term investment performance appraisal system, lengthen the investment performance appraisal cycle, determine a reasonable target return on investment.

#### *4.3 Establish personal limited investment option of occupational pension funds*

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<sup>5</sup> Human Resources and Social Security Department: "2014 Annual Human Resources and Social Security Statistical Bulletin"

<sup>6</sup> National Council for Social Security Fund: "The National Council for Social Security Fund Fund Annual Report (FY2014)."

Occupational pension accounts are personal property, though can not withdraw before retiring for other purposes, but a complete account holders should include the right to choose investment property. Clearing the right of the account owner to choose to invest occupational pension fund, on the one hand there is conducive to enhancing the personal responsibility of the pension, on the other hand can also reduce pressure on the government in terms of increasing the value of the fund.

In order to protect the security of fund , we recommend: limited investment given account holders the option that individuals can choose the investment manager in several compliance mechanism, giving up the right to choose can start the automatic default mechanism to automatically determine the default combination. Of course, the default portfolio investment risk is relatively low.

Prior to the implementation of the right to choose their individual occupational pension account, need to address issues of the unit contribution to occupational pension of account . There are two drawbacks of "Empty Account": First, it can not be invested, if the billing rates is lower than the market rate of investment, and the scale of fund account will be less than the real accumulated account, which of political risks; Second, if the accounting in accordance with the market rate of return, then formed a huge cumulative account size to do real-time at the point of retirement, the future certainly can not afford the financial burden, the system need a second reform. Thus, in the long running, it should be clear occupational pension unit pay liability and achieve real occupational pension account operations.

#### *4.4 Set guaranteed return rate*

The importance of pension investment security is self-evident, but how to operate in market that achieve profitability and can put an end to excessive investment risk? Supplementary pension insurance operations experience from the German point of view, the pre-established rate of pension fund investments guaranteed return can lock the maximum loss. In fact, when the current National Council for Social Security Fund in local commission entrusted with the management of basic pension insurance fund operations, will be in the trust agreement clearly a guaranteed return rate when the actual rate of return is lower than the guaranteed rate of return, by the trustee compensate for the loss.

## Topic 1.3.2

Combination of social pooling and individual accounts techniques in pension schemes for employees<sup>7</sup>

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<sup>7</sup> Excerpt from the report by Mr. Song Xiaowu



## **1. Pooling-Account Combination System Model of Basic Pension Insurance**

Following the basic principles for perfection of pooling-account combination system of basic pension insurance mentioned above, this report regards that Notional Defined Contribution can be implemented when it is indeed difficult to fully fund individual accounts, but only small nominal individual accounts can be implemented. Nominal individual accounts shall not be expanded. In particular, 28% of full Notional Defined Contribution shall not be implemented. Zero social pooling would make the system lose inter-generation mutual aid mechanism, which is a fundamental overturn of pooling-account combination system. It shall be clearly defined that Notional Defined Contribution is pay-as-you-go system. If the government input is not provided, the paying pressure of future aging of population cannot be eased through “actuary balance”. Therefore, this report puts forward two schemes:

### **1.1 Scheme 1: Encouraging Fund Accumulation and Fully Funding Individual Accounts in a Gradual and Flexible Manner**

It is an optimized scheme. Respect and prudently treat the common understanding formed during previous three discussions concerning individual accounts, review pooling-account combined partial fund accumulation system established by China (equal consideration to fairness and efficiency and present and long term), objectively treat the reality and causes of failure to fully fund individual accounts, and make clear that failure to fully fund individual accounts cannot deny the correctness of pooling-account combined partial fund accumulation system.

Organically combine social pooling with individual accounts, keep existing payment ratio unchanged, manage pooling accounts and individual accounts in a mixed way, and ensure paying of pension insurance in current period. Reform pension investment management system and encourage each place to accumulate pension fund. Individual account fund and its investment and operation management are in the charge of provincial government. Promote individual account pension investment and management system reform, introduce market-oriented investment operation and competition mechanism, enhance dynamic power of each place to accumulate pension fund and ensure value preservation and increase of pension fund. Pension fund accumulation, investment return and investment risks are in the charge of provincial governments. Meanwhile, separate administrative affair management, investment management and supervision management of pension insurance, strengthen pension investment and operation supervision of the central government, establish pension fund investment risk control system, and formulate specific investment objects, investment rules, procedures, etc..

As for cross-region employee flow, it can be stipulated that it is only required to transfer pension insurance relation but not required to transfer individual bookkeeping accumulation fund due to different inter-region accumulation fund scale and scale of individual accounts fully funded. Relevant individual account expenditure of pension of transferred population is solved by the central government using collection adjustment payment based on realization of nationwide pooling of basic pension and according to ratios of population transferred out and transferred in among different areas.

### **1.2 Scheme 2: Implementing Lager Social Pooling + 8% Small Notional Defined Contribution**

It is a secondary optimized scheme. Ensure that pooling-account combined basic system model remains unchanged and payment ratios of social pooling and individual accounts remain unchanged. Social pooling is formed by enterprise payments as 20% of total amount of wages. Pay-as-you-go system with payment

determined is implemented; individual accounts are formed by individuals as 8% of their wages. Bookkeeping method of Notional Defined Contribution with payment determined is implemented. Individual account pension payment and treatment are strictly corresponding, i.e. more payment for more gain. Pooling fund and individual account fund are managed and used in a “mixed” way to ensure paying in current period. The surplus can be invested and operated.

The central government is responsible for nationwide pooling of basic pension as well as relevant basic pension and transitional pension. The paying standards of basic pension are determined according to living standards of different areas. The central government stipulates national unified individual account bookkeeping interest rate and ensures that the investment return of pooling and individual account fund already accumulated by local governments is used to ensure employee pension insurance level of local regions before nationwide pooling of basic pension.

As for cross-region employee flow, since most regions adopt nominal individual accounts, it is only required to transfer pension insurance relation and record individual bookkeeping accumulation fund to place of movement. During cross-region transfer of employees in regions with individual accounts already fully funded, it is not only required to transfer pension insurance relation but also needed to transfer individual account accumulation fund. Individual account fund fully funded can be operated and management by entrusting National Council for Social Security Fund. Provincial governments are responsible for individual account fund accumulation, investment return and investment risks in regions with individual accounts fully funded.

## **2. Nationwide Pooling of Basic Pension**

It was put forward in the Third Plenary Session of the 18th Central Committee of the CPC that a system suitable for power of office and expenditure responsibility should be established and the power of office and expenditure responsibility of the central government should be properly strengthened. Nationwide public products and products with regional overflow effect shall be included in the power of office of the central government. The central government can collect a part of power of office according to factors like beneficiary scope, information availability and scale economy. Since basic pension insurance is a common power of office of the central governments and the local governments, the relation of power of office shall be gradually smoothened. This report thinks it necessary to fully mobilize initiative of the central government and the local governments and implement central-provincial two-level basic pooling architecture. The central government and the provincial governments shall jointly undertake responsibilities for pension. Since the rate in regions with relatively low enterprise payment rate is only 11%, the payment rate shall not be forcefully improved without exception. During start-up stage, 10% of social pooling fund of each place can be handed over to the central government and forms central pooling fund with current financial aid of the central finance. The central pooling fund shall be adjusted and used nationwide. Some of pooling fund and individual account fund are preserved in local governments. Each province and district shall comprehensively implement provincial pooling of fund. The provincial governments shall take charge of investing and operating pension surplus fund. In the future, enterprise payment rate of each place shall be adjusted in proper timing based on regional coordinated development of the whole country in the future to finally realize nationwide unification.

The central government and the local governments are jointly responsible for payment demand of basic pension. The payment is based on the principle of equality of citizens. The appropriated amount per capita is determined by dividing the number of retirees taking part in insurance of China from central pooling fund. The central pooling fund is used to determine the amount appropriated to each province according to number of retirees taking part in insurance and appropriated amount per capital as verified by each province. The payment demand of basic pension exceeding the appropriated amount of central pooling fund shall be in the charge of the local governments in each level. Strengthen actuary balance of two-level pooling fund and offer certain autonomous right to local governments under the precondition that the payment demand of basic pension is guaranteed.

It shall be clarified as how to determine the payment demand of basic pension. Pension substitution rate is involved. In 1952, it was put forward in *C102 - Social Security (Minimum Standards) Convention* released by International Labour Organization that the substitution rate of pension of common grown-up male labour paying pension insurance expenses for 30 years should not be lower than 40%; in 1967, *C-128-Convention for Security Treatment of the Aged, the Handicapped and the Members of the Deceased's Family* released by International Labour Organization improved this substitution rate to 45%. According to *China Social Insurance Development Annual Report 2014*, the enterprise employee pension substitution rate of China from 2009 to 2014 fluctuated around 66%, presenting a general stable operation. The substitution rate calculated in this report is based on wages for payment. Researches based on social average wages regarded that the pension substitution rate of China decline gradually and reaches about 45% at present, which basically reaches the standard stipulated in international social security instruments.

### **3. Supporting Measures for Perfection of Pooling-Account Combination System of Basic Pension Insurance**

#### **3.1 Expansion of Capital Sources beyond System**

Gradually improve the payment ratio of capital income of state-owned enterprises to supplement the gap of pension insurance fund and balance and adjust the payment of pension insurance fund. The capital income of state-owned enterprises is a part of fiscal revenue of the government. Therefore, using it as a capital source of social insurance fund is not only reasonable but also feasible. It is recommended that the capital income of central enterprises should be transferred to the central finance, while capital income from local state-owned enterprises should be transferred to local finance for filling the gap of pension insurance fund at this level. Meanwhile, establish and perfect multichannel social fund-raising mechanism (e.g. issuing of social security welfare lottery, charity stamps, charity IC cards and commemorative coins, establishing of social security donation capital, etc.), in order to expand fund-raising channels and enrich pension insurance fund. In addition, it should be clarified that National Council for Social Security Fund should have the function of balancing and adjusting payments of social security projects.

#### **3.2 Progressive Postponement of Retirement Age**

Postponement of retirement age is a feasible approach to ease financial pressure of pension. Facing the problem of aging of population, western developed countries usually handle it by postponing retirement age. Progressive postponement of retirement age can motivate payment, lower current expenditure and benefit the lightening of expenditure pressure. Good timing shall be selected to postpone retirement age. Retirement age shall be standardized first and equal consideration shall be

given to special conditions. Then, it shall be gradually advanced in small steps. Firstly, the selection of timing for postponement of retirement age shall be made clear of. Relevant researches indicate that the stage combining quick growth of scale of aging population and quick withering of working age population shall be the crucial stage for implementation of postponement of retirement<sup>8</sup>; 2. Difference of retirement age of males and females shall be narrowed and flexible retirement system shall be implemented first. As long as the employers and the labourers agree, they may continuously sign labour contracts; 3. Differentiated retirement age policies shall be adopted for different types of labourers (different types of work, levels of education, and genders). The retirement age of heavy workers shall be properly reduced, and manual workers with big labour intensity shall be allowed to retire ahead of time; 4. Practice of progressive adjustment is suitable. The retirement age may be postponed for 2-6 months every year so as to finally gradually postpone retirement age; 5. A motivation mechanism shall be established for in-service labours beyond mandatory age for retirement, and the pension part paid by enterprises for them shall be transferred into individual accounts.

### 3.3 Full Funding of Pension Insurance Payment Base Number

Since the pension insurance system reform of China accompanied with the process of wages monetization, the total amount of wages for payment was deviated from actual labour income. Compared with other countries, the total amount of wages of urban employees of China took up a relatively low ratio in GDP (continuously declined from 15.77% in 1990 to 11.30% in 1998). Later, this ratio was fluctuated and declined to 11.09% in 2007. In recent years, it was continuously improved to approximately 20%. The ratio of total amount of wages of main developed countries in GDP was basically around 50%. Therefore, in order to fully fund pension insurance payment base number, the gap between wage income and labour income shall be solved first. In addition, allowance subsidy system shall be standardized and management of total amount of wages shall be strengthened. Secondly, stick to social average wages as payment base number. The enterprise payment base number of urban employee pension insurance of China is social average wages, while the individual payment base number is 60%-300% of social average wages. This provision itself has the function of adjustment of income distribution. A certain viewpoint proposes to cancel concept of social average wages and fully use individual wage income as payment base number. Enterprise payments are also included in individual accounts according to ratios of individual wages of employees, which make the accumulated amount of individual accounts closely related to individual wage income. If 28% of full account system is implemented, it will undoubtedly further expand the gap of wages preliminarily distributed to redistribution field of social insurance. Therefore, enterprise payment base number shall still be social average wages. However, the statistical calibre of social average wages shall be perfected. The wage income of employees of private enterprises shall be included in the statistical category of social average wages; thirdly, under the condition of nationwide pooling of basic pension, payment rate shall be gradually lowered. Reduction of payment rate is closely related to individual accounts. If nominal accounts are implemented, the space for reduction of current payment rate will be increased. However, under the background of aging of population, long-term rate will increase without fund-raising beyond the system; if individual accounts are fully funded, the space for reduction of current payment rate will not be big, but a relatively stable rate can be maintained in a long term.

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<sup>8</sup>Tang Ruida & Guo Xiuyun. Dynamic Study of Retirement Age Based on Reasonable Supporting Ratio: Model and Simulation. *Social Security Studies*, 2014 (1).

### **3.4 Institutionalization of Treatment Adjustment Mechanism**

Establish a “three links” adjustment mechanism from system supply and demand to replace administrative adjustment. Firstly, basic pension insurance shall ensure the basic life of the insured. The pension shall be adjusted according to growth rate of consumer price index (CPI); secondly, it shall be ensured that the retirees properly share economic and social development achievements. Treatment gap among systems and groups of people shall be adjusted based on growth rate of CPI and according to the principle that the growth speed of pension shall be generally lower than growth speed of social average wages; thirdly, principle of actuary balance shall be introduced to basic pension insurance system to make the system rely on its financial balance more. If the fund paying capacity or financial paying capacity is greater than or equal to adjusted amount, the adjustment capacity can be fully provided, and full-amount adjustment is available as demanded; fourthly, “guaranteed index” ensuring certain pension substitution rate level shall be established. It can be linked with investment return of national social security fund. It can be used as a supporting policy for principle of pension actuary balance to make up the risk of decline of pension payment level resulting from adjustment of indexation; fifthly, the number of months for calculation and paying of pension in individual accounts released in 2005 shall be timely revised. The life expectancy of population shall be calculated in a scientific way according to remaining life expectancy per capita after retirement. In addition, the changing conditions of life expectancy of population and retirement age shall be fully reflected.

### **3.5 Enhancing of Openness and Transparency of Pension Insurance System**

Degree of familiarity of social public with basic pension insurance system is an important factor influencing the initiative of individual to take part in pension insurance. Therefore, the openness and the degree of transparency of relevant policies and knowledge concerning basic pension insurance shall be enhanced. Clear and simple individual pension treatment actuary formula shall be established and released to enable the insured residents to conveniently learn the relation between individual payment and treatment and make clear of ratio of individual payments used for pooling and accumulation. The annual appropriated amount per capita in the charge of pooling fund of the central government shall be clarified according to nationwide pooling scheme of basic pension, which has made clear of responsibilities of the central government and the local governments for determination of pension of single insured resident so as to provide clear basis for pension transfer and renewing, effectively supervise the governments and prevent corruption of micro powers like social insurance.

## Topic 1.3.4

Multi-tiered design of pension system<sup>9</sup>

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<sup>9</sup> Excerpt from the report by Mr. Dong Keyong

## 1. The calculation results of fund balance

According to the results of simulation and calculation of this report, under the current population policy, the current basic pension system will start to experience fiscal deficit in its social pooling funds from 2025, and the balance will be exhausted by 2028. The overall system will not be able to make ends meet. However, if the reform plan is thoroughly implemented, the fiscal deficit in the social pooling funds will not occur until 2034 and the system would remain financially sustainable until 2047. Obviously, the reform of the public pension system can effectively resolve the issue of insufficient funding, improve the sustainability of public pensions, and reduce the government's financial burden.

## 2. Simulation calculation of relative payment level of individual account

Generally speaking, given the payment rate as well as the other parameters the rate of replacement can be calculated from the model discussed above. If the parameters change, such as the nominal return on investment, the replacement rate will be changed. According to the report of the simulation calculations, under the recent reform scheme that defines individual account payment rate at 8%, if the rate of return on investment reaches 6%, the payment level will reach 30.8%. This is then coupled with the benefit level of public pension, which is 40%; hence the overall level of benefit will remain at around 70%, which is basically equal to current payment level. In the mid - and long-term plan, which sets individual account payment rate at 8%, as the rate of return on investment reaches 7%, it is expected that the benefit level of individual account pension arrives at 39%. With the public pension providing additional 30%, the overall level of payment is about 69% which is still of the same level with the current payment level.

## 3 Diversifying the means of realisation for state-owned assets

Considering the potential impacts on the market from direct transfer of state-owned shares to the personal account, as well as the complexity of specific operative procedures for each individual account such as equity allocation, it is necessary to adopt various alternative means: for instance to first transfer the holdings and then reduce the holdings step by step.

### *3.1 Means to transfer the holding of state-owned assets*

First, transfer the holding of state-owned assets to the pension fund management institution. In order to maintain the state ownership, it is feasible to transfer the holdings possessed by SASAC basic pension insurance management institutions, which could be NCSSF-National Council for Social Security Fund and could also be a pension management agency (PMA). It should be noted that, in order to ensure the stability and steady development of listed state-owned enterprises, it is important that, in the case of shares have been allocated, the rights as shareholders are still under the exercise of the SASAC (State-owned Assets Supervision and Administration Commission of the State Council) on behalf of the companies.

### *3.2 Means to reduce the holding of state-owned assets*

The second step is to substantiate individual accounts through equity pledge together cash advance from MoF and Commercial banks in the form of bonds and commercial loans. There are two possible approaches. The first is to have the MoF issue special bonds to the People's Bank of China or commercial banks directly so as to obtain cash to inject into the personal accounts. Next, the PMA hand in the returns of holdings reduction and stock interests to MoF for the redemption of special treasury bonds. After the personal accounts are substantiated, it is necessary to establish market mechanism for the operation through asset allocation. Considering the risks involved in the marketization of the operation of the individual account,

we can opt for the second solution. First, PMA pledges the transferred holdings of state-owned shares to the MoF, who will make cash loans from the PBC and commercial banks, and then lend cash to PMA. After obtaining bank loans, PMA could allocate the funds to each individual account according to participants' contribution. At the same time, the MoF issues special treasury bonds, which can be held by the individual account through cash purchase, and the MoF will pay back the loan of the people's bank or commercial bank with the such funding PMA will use the reduction and returns of holdings to clear the debt with the MoF, who will use the acquired cash for the redemption of bonds held by individual accounts. In the meantime, individual accounts will have investment in special treasury bonds. As the bonds are redeemed, personal accounts enjoy cash income, gradually begin to diversify asset allocation, and achieve marketization.

#### **4 The determination and payment of benefits for social groups 'in transition'**

##### *4.1 Defining payment level for the old workers and the new workers*

During the 1997 reform, three categories of people have been formed. First participants in job market after the implementation of the reform are commonly referred to as the "new worker". Another group consists of those who retired before the implementation of the reform called the "old worker". Finally there is also the third group, who started work before the reform and retired after the reform called the "middle worker". The three-pillar reform focused on individual accounts will inevitably have disparate impacts on these groups. "The old worker" having retired before 1997, has no business with personal account, so the reform has very little effects on them. But considering the phenomenon of 'the earlier retirement the lower the benefit', it is suggested that preferential policy arrangements be applied to 'the old workers' and raise the payment level for this group. As for the new workers who started work after the 1997 reform, the individual accounts will all be fully substantiated, and the payment after retirement will not involve the issue of 'transition'.

##### *4.2 Determining the Payment level for "middle worker" during the transition*

As for those "middle worker" who took part in the workforce before 1997 and retired after the implementation of the three-pillar pension system, their individual accounts are substantiated after the year of 1997. However, there will be inadequate reserve in the individual account prior to 1997. As the benefit of public pension declines, such inadequacies will potentially insufficient social protection for life after retirement. We believe that the "middle worker" should be compensated for loss of benefits in the reform process to promote the smooth progress of the reform. Specifically, one possible means is to set a target replacement rate, for instance 70% as proposed in this report. For the "middle workers", the overall replacement rate of public pension and individual account combined that is enjoyed by each individual should be evaluated. If it does not reach the target level of 70%, the discrepancy should be addressed by state subsidy. Since the inadequate reserve of individual accounts among "middle workers" is attributable to the structural transition, the fund required to fill in the gap should be provided by state finance, through the means of direct payment of current budget or separate compensation fund established during the transfer of state-owned assets to substantiate personal accounts.

#### **5.5 Assessment of the NDC model in the basic pension system in China**

Firstly, NDC leads to weakening the function of redistribution, which is difficult to resolve. The pension payment level under nominal personal pension account system is entirely determined by individual contributions and periods of contribution. It's a similar pattern to Singapore's Central Provident Fund, which lacks the function of income redistribution among participants. Under such arrangement, public



pension cannot realise the mutual assistance and the promotion of equity. To address the issue, Sweden provides compensation through the separate 'zero pillar'. By comparison, there is only public pension in China with redistributive function, and the national annuity as the zero pillar is still absent. It would be expected that if NDC is adopted for the pension system, the income disparity among the retirees will deepen, and the basic livelihoods of some elders groups will be hard to sustain. Secondly, retirees cannot afford the decrease of payment level caused by the implementation of NDC system. Different from Sweden's pension system, which enjoys proper structure, multiple funding sources and high payment, China's old-age pension system is dominated by the basic old-age insurance. Enterprise annuity suffers from the lack of development for a long time. Elderly care is highly dependent on the basic old-age insurance. After eleven rises of payment level, the benefit of basic old-age insurance is still around 45% or so, and remains close to the bottom line established by the International Labour Organization. In this context, if the NDCs reform is implemented, further decline in the level of benefit is expected as account interest rate is lower than the actual rate in the long term, and many retirees are at the risk of falling into poverty. Thirdly, the size of balance in the pension fund is quite limited in China; hence it is difficult for the fund to increment through investment under NDC. In Sweden, after the NDC reform, the current balance of pension fund is incremented through professional investment, and a part of increments goes into the benefit of participants whereas the other goes back to the fund to cope with the high level of payments in the long run. This mechanism lies at the core of NDC system. In 2013, the balance of nominal accounts in Sweden is 43% of the total amount of salary, which is of very large scale given the high wage level in Sweden. Despite the fluctuation of proceeds, in the long run, the returns of investment also constitute an essential source of funding. However in the Chinese context, the balance of pension fund is of very small size at only 3.5 trillion, which can only maintain only the payment of 16 months. Even if used for investments, the return on investment will still be incommensurate with the size and growth rate of the payment; hence the support will be very limited. Under NDC arrangement, it is difficult to alleviate the pressure on payment of pension through pension fund investment without substantiating individual accounts. Finally, the rate of charge is volatile, which will influence the participants' expectation for the stability of pension payment. As mentioned above, under NDC mode, if personal account has no balance, the determination of account interest rate will mean the indebtedness of the government to individual accounts. The determination of account interest rate has significant bearings on the rights of individuals and the government responsibility in the future, hence is essential to the design of NDC system. It is dependent on economic growth, the increase in wage, inflation, and the balance of pension fund, hence is in constant fluctuation every year, which will inevitably increase the volatility in the accumulation of pension among participants. In cases of special account interests being adopted for automatic balance mechanism, there might even be diminishment in the pension fund. Also in Sweden, for example, in 2010 Sweden, due to overall imbalance of the old-age insurance system, the automatic balancing mechanism was initiated. As a result the growth rate of pension decreased from 4.6% down to 3%, and further down to -4.3% in 2011. This is disadvantageous for the establishment of stable expectation among participants, or for them to make well informed plans for the life after retirement. However, Sweden only has a 5.7-million population, and its pension system is relatively uniform, which means less difficulty for policy adjustments and management. But in China, the basic old-age insurance covers more than 0.3 billion employees. On top of that there is a huge regional disparity between the Western and the Coastal regions. Under such condition, imprecise determination of account interest rate could lead to the situations where the pension rights of certain groups unguaranteed.

Therefore, in general, the NDC system, though have been practiced and succeeded in some countries, is not applicable in China which lacks the institutional foundation for a transition to a NDC-based pension system.



## **PROJECT RESULT 5**

### **Reform efforts in response to Urbanization trends**

### Topic 1.4.3

#### Strategy of integrating social security system in urban and rural context<sup>10</sup>

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  - 3.3 Improve the policies on transfer and continuation of credentials of basic pension insurance for urban employees 47**
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<sup>10</sup> Excerpt from the report by Mr. Wang Zeying

## 1. Overall thinking

Efforts should be made to implement the spirits of the Eighteenth National People's Congress and the Second, Third and Fourth Plenary Sessions of the Eighteenth Communist Party of China Central Committee, follow the overall requirements of comprehensive deepening of reform and comprehensive ruling by law, center on the overall objectives of building comprehensively a moderately prosperous society, adhere to the principles of nationwide coverage, basic security, and multilevel and sustainable development, focus on improving fairness, adapt to mobility and securing sustainability, advance the multilevel construction of pension insurance system, further integrate and improve the basic pension insurance system, improve the measures on pension insurance transfer and continuation, raise the overall planning level, enhance agency capacity building and establish a nationally unified pension insurance information system.

## 2. Integrate basic pension insurance systems further

Efforts should be made to integrate the basic pension insurance system for urban enterprise employees and the pension insurance system for state organs and public institutions into a unified basic pension insurance system for urban employees, promote institutional fairness and remove the barriers between the said two pension insurance systems.

Basic assumptions: The staff members of urban state organs and public institutions, flexible employees and foreigners who get employed in China should be covered; The institutional pattern that combines "social pooling and personal account" should be implemented; Employers should pay 20% of the overall wage and individuals shall pay 8% of personal wage as pension insurance premium; The pooling fund should be composed of employer payment and fiscal subsidy and the personal account should be made up of individual payment and investment income; The pension for retirees should consist of basic pension, transitional pension and pension of personal account. The basic monthly pension for retirement should be 1% of the mean value of the local monthly average wage of on-post employees in the previous year and the personal index-based monthly average wage, on which the payment of premium is based, for every full year of payment. The monthly pension of personal account should be the amount of deposit in personal account divided by the number of months of pension payment, which is determined according to the average life expectancy of urban populations at the retirement, the retirement age of the individual and the interest. The amount of pension should be adjusted year on year.

The measures on payment of transitional pensions as specified in the pension insurance system for state organs and public institutions and the pension insurance system for enterprise employees should remain unchanged.

The payments of staff members and the pensions of retirees of state organs and public institutions and enterprises (including flexible employees and contracted employees of state organs and public institutions) should be accounted independently in order to prevent the funds of pension insurance for state organs and public institutions from embezzling or occupying the surplus of funds of pension insurance for urban enterprise employees and to divide reasonably the payment and supplementation responsibilities of

finance in the operation and management of pension insurance system for state organs and public institutions.

### **3. Improve the policies regarding basic pension insurance**

According to the *Social Insurance Law*, the government shall bear the basic pension insurance premiums payable during the deemed period of payment and the cost for transition of basic pension insurance for urban enterprise employees and state organs and public institutions shall be raised through various channels to facilitate institutional fairness. Efforts should be made to improve personal account policies and raise the interest for personal account to attract long-term individual payments. Besides, pension adjustment mechanism should be improved and the factor of payment years should be taken into consideration to make the insured more active about constant payment. Age of retirement and the minimum number of payment years for obtaining pensions should be raised gradually. In addition, the following improvements should be made.

#### **3.1 Promulgate policies to encourage urban and rural residents to voluntarily participate in the basic pension insurance for urban enterprise employees**

Policies should be promulgated to encourage urban and rural residents to voluntarily participate in the basic pension insurance for urban enterprise employees. Urban and rural residents should be allowed to choose the basic pension insurance for urban employees according to their personal and household income and bearing capacity in the identity of flexible employees and to enjoy the fiscal subsidy for individual payment as per the policies on basic pension insurance for urban and rural residents.

#### **3.2 Improve the policies on the integration of urban and rural pension insurance systems**

Efforts should be made to safeguard the pension insurance interest of migrant workers and other employees flowing between urban and rural areas and improve the policies for connecting the basic pension insurance for urban enterprise employees and the basic pension insurance for urban and rural residents in the principle of fairness and convenience. Besides, the *Interim Measures on the Integration of Urban and Rural Pension Insurance Systems* should be adjusted. As for the people who participate in both the said insurance systems and have reached the statutory retirement age for the pension insurance for urban employees:

(1) If the insurant has paid the premium for the pension insurance for urban employees for 15 or more years (or the extended payment reaches 15 years) and transfers from the basic pension insurance for urban and rural residents to the basic pension insurance for urban employees, the deposit of personal account should be calculated on a consolidated basis and the number of years of payment for pension insurance for urban and rural residents should not be calculated on a cumulative basis; or the deposit of the personal account for the basic pension insurance for urban and rural residents may be converted, according to payments of flexible employees over the years, into the number of years of payment for pension insurance for urban employees and the personal account may be included into pooling fund and personal account respectively; or the pooling payments may be supplemented according to the insurance payment standard for flexible employees and the number of years of payment for pension insurance for urban and rural residents may be calculated on a consolidated basis. Pension should be paid according to the policies on the basic pension insurance for urban employees.

(2) If insurant has paid the premium of the basic pension insurance for urban employees for fewer than 15 years, the insurant may apply for transferring from the basic pension insurance for urban employees into the basic pension insurance for urban and rural residents, the entire deposit of the personal account for pension insurance for urban employees and 12% of employer payment over the years and its interest should be included into the personal account of pension insurance for urban and rural residents, the number of years of payment for pension insurance for urban employees should be converted on a consolidated basis into the number of years of payment for pension insurance for urban and rural residents. After meeting the conditions for obtaining the benefits of pension insurance for urban and rural residents, the insurant should obtain the benefits as per the measures on the pension insurance for urban and rural residents. If having paid the premium of pension insurance for urban employees for fewer than 15 years, the insurant may also convert the entire deposit in the personal account of pension insurance for urban and rural residents into the number of years of payment for pension insurance for urban employees according to the payment of a flexible employee over the years; or supplement the pooling payment according to the payment of a flexible employee over the years and calculate the number of years of payment of pension insurance for urban and rural residents on a consolidated basis. If the cumulative number of years of payment is smaller than 15, the payment can be extended for 5 or fewer years. If it is still smaller than 15 after the payment is extended for 5 years, the residual payment may be supplemented in a lump sum.

### **3.3 Improve the policies on transfer and continuation of credentials of basic pension insurance for urban employees**

At first, the deemed years of payment should be normalized and defined further, the refund and disposal of repeated payments should be normalized and the measures on disposal of temporary payment accounts should be improved. Furthermore, in the transfer of funds, the accounts should consist with the actual funds and information flows should synchronize with fund flows. One fund should be transferred or a person and one fund for several people or one people with several funds should be avoided. Pooling fund should be transferred along with personal account. Finally, the measures on delayed payment, supplemented payment and prepayment should be improved. Migrant workers who get employed in urban areas, native or not, should be allowed to participate in the pension insurance according to the policies applicable to individual business owners and flexible employees. After cancelling or terminating the labor relationship with their employers, the insured should be allowed to continue paying insurance premiums as flexible employees and participate in the pension insurance for urban enterprise employees in the principle of free will.

## **4. Rise the overall planning level of basic pension insurance**

Nationwide planning is the statutory objective as specified in the social insurance law as well as the objective need for building a unified labor force market, narrowing the gap of economic and social development among regions and equalizing public service. It can remove the problems regarding the pension insurance relation transfer and interest security of employees flowing among different regions and improve the bearing capacity and usage rate of funds.

Basic pensions of basic pension insurance for urban employees should be planned as a whole in China. Efforts should be made to divide reasonably the responsibilities between the central government and the local governments and classify the present basic pensions into national basic pension and regional additional pension. The national basic pension should consist of the fund raised by the central government according to the number of on-post employees of each province and the unified payment standards and

the central government subsidy and be paid according to unified standards and the number of retirees of each province. The central finance should be responsible for the supplementation and the central government should control the budget of basic pensions. Regarding regional additional pension, local governments should raise the funds and pay and adjust the benefits and local finance should be responsible for the supplementation. The powers of office and finance of the central government and the local governments should be defined and the central government and the local governments should support jointly the steady operation of pension insurance systems and funds.

The overall planning level of basic pension insurance for urban and rural residents should be raised gradually. On the basis of promoting provincial planning, efforts should be made to realize national planning. At first, efforts should be made to facilitate the provincially unified management of basic pension insurance funds for urban and rural residents, centralize the data of the province, provide social insurance service locally, conduct supervision at provincial and municipal levels and realize provincially unified management of personal account funds. Then, efforts should be made to unify the levels of basic pensions and personal account subsidies gradually within every province, propel the nationally centralized management of basic pension insurance funds for urban and rural residents, centralize all data, provide social insurance service in every prescribed region, conduct supervision and central and provincial levels and realize nationally unified management of personal account funds.

## **5. Improve the capacity of pension insurance operation management service**

Pension insurance operation management regulations should be sorted and operation service resources should be integrated. Efforts should be made to integrate gradually the basic pension insurance for urban enterprise employees, the basic pension insurance for state organs and public institutions and the basic pension insurance for urban and rural residents into one organization for management, steadily facilitate the vertical management of pension insurance and provide support for the integration of basic pension insurance systems and the raising of planning level. Active attempts should be made to administer vertically the pension insurance agencies below the provincial level and improve gradually relevant administrative measures as per the *Social Insurance Law* and in the principles of “safety, effectiveness and authoritativeness”. Furthermore, efforts should be made to start with the vertical management of service where the vertical management conditions are not met. First, the authority of administering the pension insurance funds and service data should be improved to the provincial level and the unified dispatching of funds and centralized management of data should be strengthened. Then, the vertical management at the provincial level should be promoted in due time.

The construction of basic-level public service platforms should be enhanced. Full play should be given to the governments and the society and efforts should be made to integrate and utilize the network and service resources of basic-level service organizations and social service institutions, establish employment and social insurance service platforms in all sub-districts, villages and towns of China, strive to set up employment and social insurance service stations in all communities and administrative villages and implement the social insurance assistant system generally in administrative villages; and improve the operation management service network with the focus on cities (including counties and districts) and on the basis of sub-districts (towns), communities (administrative villages) and other basic-level service network stations.

The standardization and normalization of pension insurance service agencies should be facilitated and the agency service for transfer and continuation of urban and rural pension insurance should be normalized.



On the one hand, efforts should be made to reinforce further the foundation of the agency service, normalize the records of pension insurance interest, sort the archives of insurants and ensure the completeness and consistency of information. On the other hand, efforts should be made to establish provincial-level transfer and continuation service centers, transfer pension insurance credentials from a province to another. Problems of a province should be solved within it.

Efforts should be made to enhance social insurance supervision, normalize the purchase of insurance and encourage migrant workers to participate in pension insurance.

## **6. Strengthen the promotion of information technology**

While the policies on the integration are improved, the nationally unified pension insurance information system should be advanced to realize electronic transfer and continuation.

Firstly, such infrastructure as the “Golden Insurance Project” should be promoted and utilized proactively, the construction of the national unified information system should be accelerated, the standards on pension insurance service data should be unified, the data should be sorted and a feasible data sharing mechanism should be formulated. Besides, social insurance card management should be realized, social insurance cards should be distributed to all objects of service and the multi-functional and generally used social insurance cards, through which the insured can pay the premiums, inquire the payment information and obtain insurance benefits, should be popularized. In addition, basic standards for “electronic social insurance” service should be formulated, the whole-people insurance registration system and the national service system for online inquiry of records of individual rights and interests as well as the trans-provincial pension insurance transfer and continuation system and the trans-regional pension insurance management system should be established. The function of comparing the trans-system repeated payments should be added to the information system. Secondly, promotion of regional access to network should be accelerated and the nationwide network for trans-provincial transfer and continuation should be realized as soon as possible. Thirdly, the application of the transfer and continuation information system should be propelled further and local service systems and trans-regional transfer systems should be connected closely to ensure service operation. Fourthly, existing functions of the system should be improved and functional defects should be rectified. Finally, intensified trainings should be provided to the staff members of social insurance agencies to have them familiar with the functions and operation of the transfer and continuation information platform.