Pension Insurance in China

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Pension Insurance Reform in China

- Economic Reform and “Opening Up” policy of China in late 70’s.
- PAYG shift from district to provincial level in order to ensure fair competition among State-Owned Enterprises (population of most provinces is equal to or exceeds the population of some countries).
- Coverage expanded to all enterprise employees (rural workers and migrants are not covered).
- Mandatory accumulation fund with individual accounts is established in each province.

System Model and Legal Base - Basic Pension Insurance for Enterprise Employees (BPIEE)

- Solidarity component – social pooling at provincial level.
- Mandatory accumulation component – the individual account system (Pillar II)
- Pension benefit consists of two parts – solidarity and accumulation
- State Council (Parliament) Notification on "Furthering Pension Insurance Reform for Enterprise Employees"
- State Council Decision on "Establishing a Unified Basic Old-age Insurance System in Enterprises" (Social pooling at the national level may start on pilot basis in 2012)

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Coverage & Financing (BPIEE)

- Intended coverage:
  - employers and employees of all urban enterprises
  - casual workers and self-employed
  - Village and Town Enterprise workers (on voluntary basis)
- Employers and employees pay contributions monthly.
- Government subsidizes basic pension insurance.

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Benefits and Qualification for Benefits - (BPIEE)

- **Complex benefit formula**

  – half of the contributor's indexed wage plus the average local wage for the previous year adjusted for years of contributory service
  plus
  - individual account balance / 120
- **Qualifying conditions**
  - 60 for men and 50 or 55 for women
  - 5 years concession for workers in special posts
  - 5 years concession for redundant workers
  - minimum of 15 years contributions

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Individual Account - BPIEE

- Introduction of individual account in early 1990s
- Changes in contribution rate. Currently employees contribution rate is 8%
- Notional account
- Efforts to turn notional individual account into funded account

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Basic Pension Insurance for Employees of Public Institutions –Civil Servants and military (BPIEPI)

Slow progress in BPIEPI reform

- Similarities with and differences from BPIEE (pension benefit consists of a solidarity part and accumulation part)
- Challenges to BPIEPI

- Limited coverage and small size of funding
- Financing difficulties in poor areas

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Rural Pension Insurance

- Origin of the new rural pension insurance system
- Similarities with but differences from the basic pension insurance for enterprise employees

- Partly funded system with social pooling and an individual account
- Subsidies from local government and Village and Town Enterprises towards farmers' contributions
- Farmers over 60 years receiving benefit payment

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Supplementary Pension System - Enterprise Annuity (Corporate Funds) – 3rd pillar

- Enterprises covered by BPIEE and having no contribution arrears may establish an enterprise annuity (corporate fund).
- Collective agreement must be signed between employers and employee representatives.
- Detailed annuity plan must be submitted to the Ministry of Human Resources and Social Security for record.

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Scheme Requirements

- Contributions are made by both employers and employees
- Annuity account management must be sub-contracted to qualified fund managers
- Benefit shall be paid upon retirement in two different models specified in the annuity plan.

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Fund Management & Regulations

- Fund management responsibilities are delegated to the trustee.
- The trustee sub-contracts account management and investment management to qualified professional institutions.
- The Ministry of Human Resources and Social Security (MoHRSS) and fund regulatory institutions promulgate relevant regulations.

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Investment Principles and Supervision

- Fund safety is the first condition.
- The yield of interest is also an important consideration.
- Liquidity is least important.
- MoHRSS has primary responsibility for management supervision together with the Chinese fund management regulatory institutions.

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The Social Security Fund (SSF)

- SSF established as a strategic reserve to cushion the impact of population ageing on social security.
- It is financed by the central government and administered by SSF National Council.
- SSF National Council not only makes direct investments but also sub-contracts professional institutions for investment.
- Similar supervisory and regulatory mechanisms apply to SSF investments as for enterprises

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Pension Insurance Administration

- China's pension insurance administration is centralized on the provincial government level
- 5 main risks are covered by the social insurance administration – pension, occupational injury, sickness and maternity, unemployment and medical insurances
- Community-based services are promoted to ease the burden on core staff.
- Staff and operational costs are met by the Chinese government.

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Experience and Lessons Learnt

- Reform programs and initiatives have to be carefully developed and tested on a pilot project basis.
- Administration is the key to success of the new social insurance system.
- Investment of long term funds like the individual account must be sub-contracted to professional institutions.
- Decentralization is a double-edged sword. If supervised and regulated properly, decentralized management contributes to improved efficiency and client satisfaction. However, the management cost is usually higher without economies of scale.

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