

Expanding Social Insurance Coverage to Informal Workers

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Challenge

- Governments in developing countries seek to create programs that help citizens cope with major risks and ensure adequate living standards in old age
- Difficult to expand social insurance program coverage when much of the economy is unregulated (unorganized sector)
- Design features of SI programs can increase informality!

Outline

- Policy options for expanding coverage
 - Benefits and drawbacks of different design features
- Chinese case
- Lessons for India and other developing countries

Policy Options

- Mandatory contributory insurance (CI) programs
 - Always been main type of SI
 - Usually financed by employers and workers (usually as a share of wage)
- Voluntary contributory insurance programs
 - Can include matching subsidies by government
- Non-contributory Insurance (NI) programs (social pensions)
 - Funded by sources other than from employers and workers (directly)
 - Often targeted
 - Can be universal (UI) if cover entire population with universal benefit packages

Key Pension Design Features

For CI programs:

- Contribution rates (as share of wage)
- Defined benefit (DB) versus defined contribution (DC) programs
- For DB systems, benefit rules (redistribution, e.g., minimum pensions)
- Portability of benefits

For NI programs:

- Amount of benefits
- Eligibility rules, especially age

*All choices have budget requirements/implications!

CI Program Design Considerations

- High contribution rates create incentives for evasion and greater informality
 - Compliance a major issue in developing countries
 - Depends on perceived value of the benefits
 - In immature systems, workers may be skeptical about program administration, and future benefits
 - For pensions, DC systems may increase perceived value of benefits, but reduces ability to redistribute
 - Portability of benefits
 - Constrains optimal household resource allocation:
 - Pension contribution rate may be higher than desired savings rate, illiquidity undermines precautionary saving role

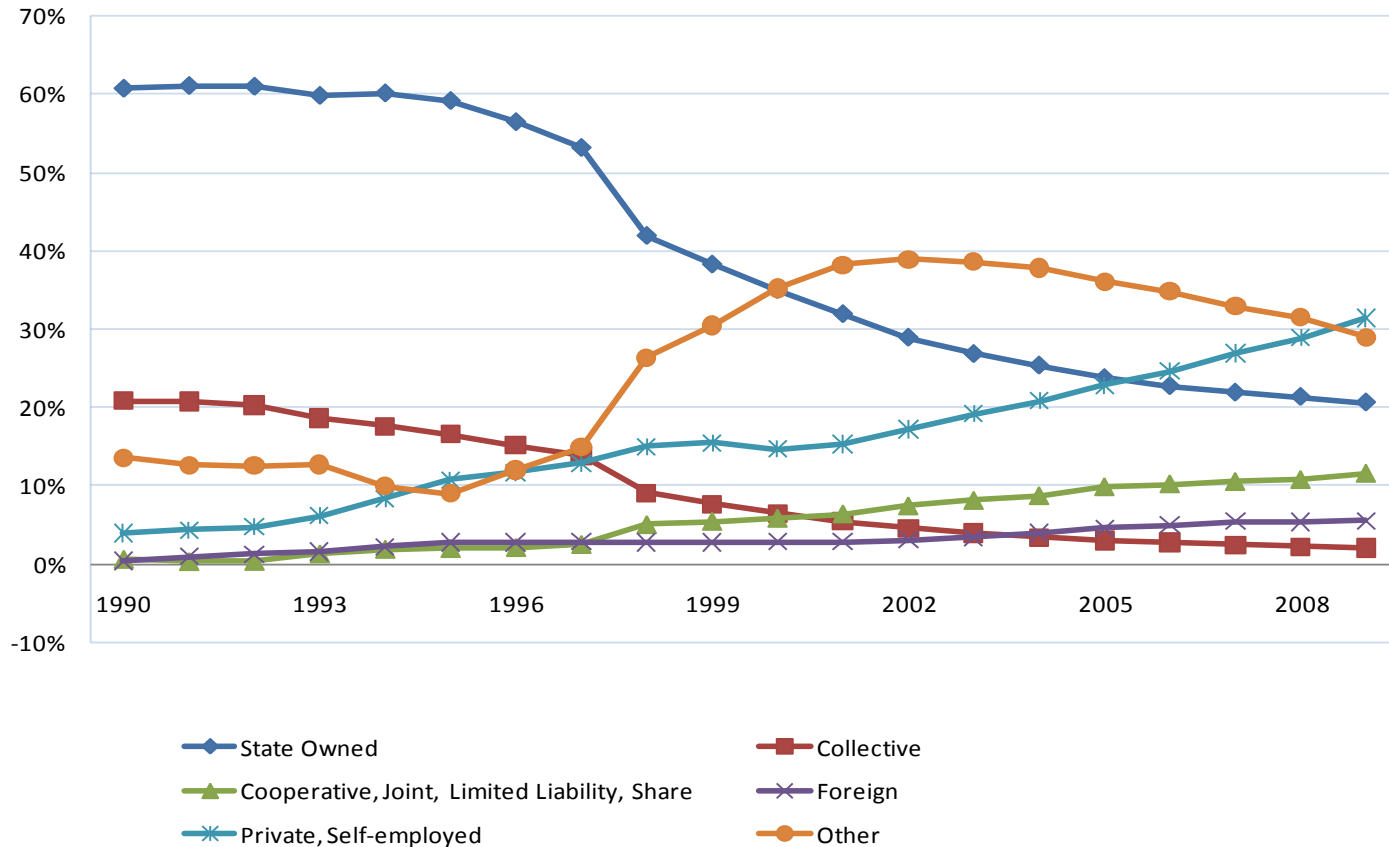
NI Design Considerations

- May undermine incentives to participate in CI programs which provide greater benefits
 - Less of a problem if formal sector jobs highly rationed (workers won't leave high-paying jobs)
 - Incentives lower if benefit levels lower, eligibility rules narrower
- Level of NI program benefits creates an income/wealth effect that can reduce work incentives
- Should consider how NI programs work in conjunction with other social assistance programs targeting the poor

Chinese Case

- Benefited from less informality initially due to socialist legacy (esp. in urban areas)
- Main programs are traditional CI DB programs
- Rising informality over time with rise of migration and private sector
- New labor regulations protective of workers, requires employers to provide labor contracts and SI benefits
- Recent expansion of NI/voluntary CI programs to cover nearly the entire population, including in rural areas
- But many problems and challenges.....

Composition of urban employment, 1990-2009



Detailed surveys in 6 large cities finds **84% of local resident workers and 39% of migrant workers are covered** by at least one of the main three social insurance programs in 2009.

Table 1. Intended Beneficiaries of Social Insurance Schemes in Urban China.

	Pension Insurance	Unemployment Insurance	Medical Insurance	Work-Injury Insurance	Maternity Insurance
<i>Social insurance schemes for urban wage-based workers</i>					
Public institution employees	T	M	M	T	T
Civil servants	T	T	M	T	T
Urban enterprise workers	M	M	M	M	M
Self-employed individuals	V		M	V	
Informal employment	V	V	V	V/M	
Rural migrant workers	V	V	V	V/M	
Unemployed workers	V		V		
<i>Social insurance schemes for urban residents</i>					
Urban residents	V		M		

Notes: (1) Urban enterprises include SOEs; collective units; joint ownership; limited liability and share holding companies; foreign, Hong Kong, Macao, and Taiwan funded enterprises; private enterprises. (2) M, mandatory by the Social Insurance Law and policies; V, voluntary by the Social Insurance Law and policies; T, traditional defined benefit approach. (3) Unemployment insurance, work-injury insurance, and maternity insurance do not apply to urban residents.

Health Insurance Coverage on Working Age Adults, by Gender and Residence Status

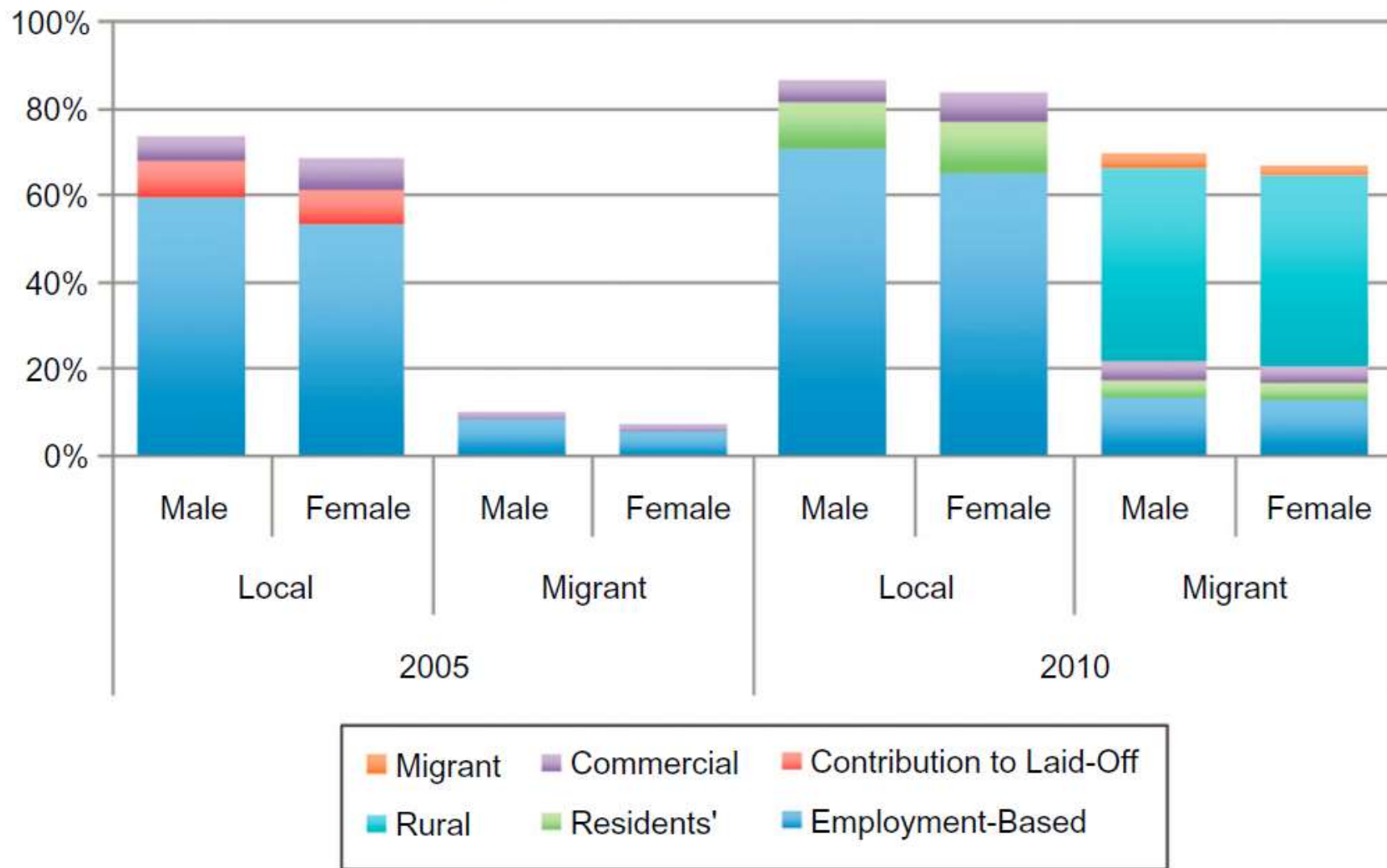


Fig. 4. Health Insurance Coverage in 2005 and 2010: Increases in both Employer-Provided Health Insurance and Access to NRCMS Insurance. *Source:* Five City Samples from the China Urban Labor Surveys (2005, 2010).

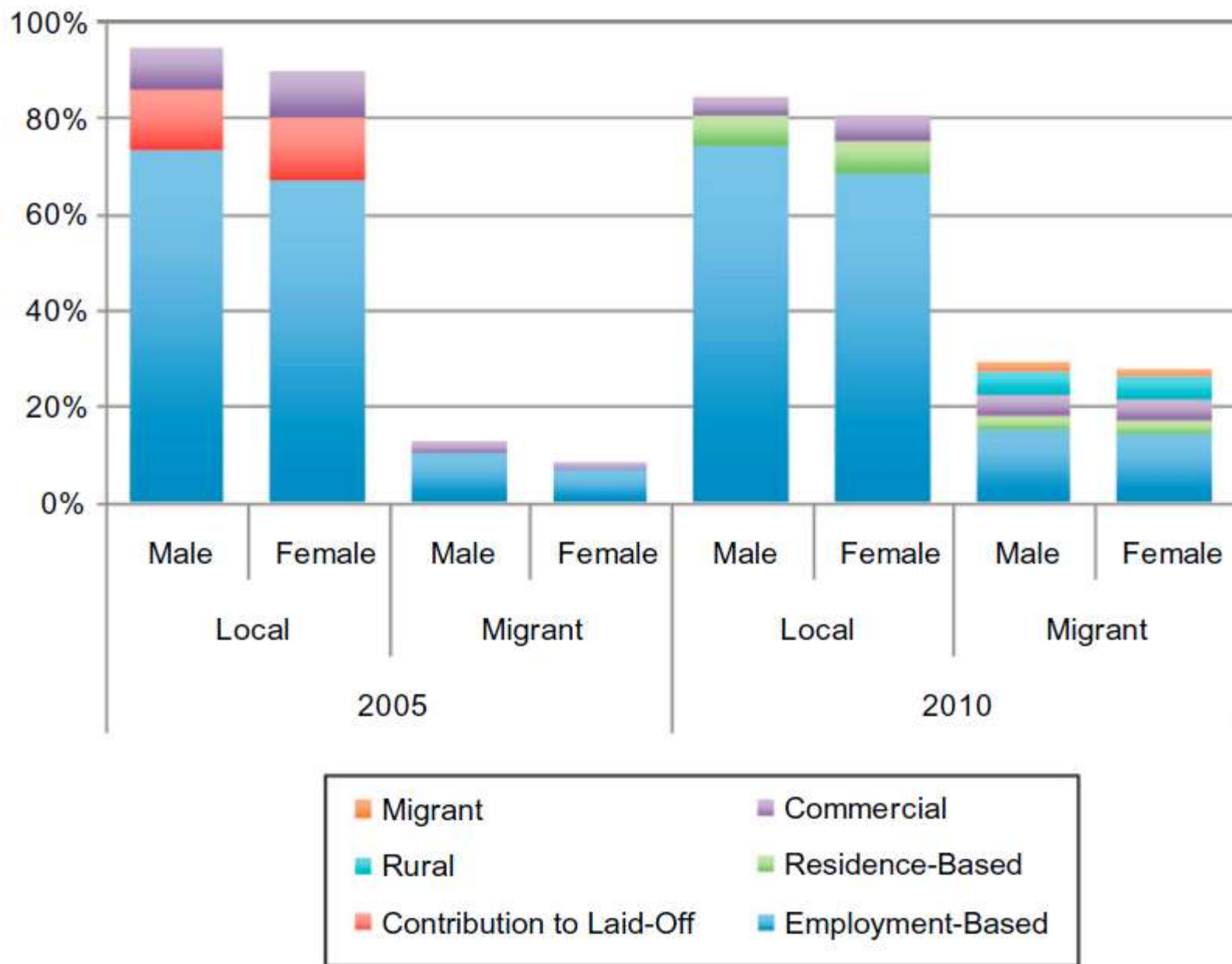


Fig. 2. Pension Coverage of Working Age Adults, by Gender and Residence Status
Source: China urban labor survey (2005, 2010).

China's CI programs have very high contribution rates

Table 3. Urban Social Insurance Contribution Rates for Urban Enterprise Workers.

Type	Employer	Employee
Pension insurance	20% of payroll	8% of monthly wage
Unemployment insurance	2% of payroll	1% of monthly wage
Medical insurance	6% of payroll	2% of monthly wage
Work-injury insurance	0.5–2% of payroll	No contribution
Maternity insurance	0.5–1% of payroll	No contribution
Total	29–31% of payroll	11% of monthly wage

Source: Authors' compilation according to relevant policy directives and documents.

From Giles, Wang, and Park (2013)

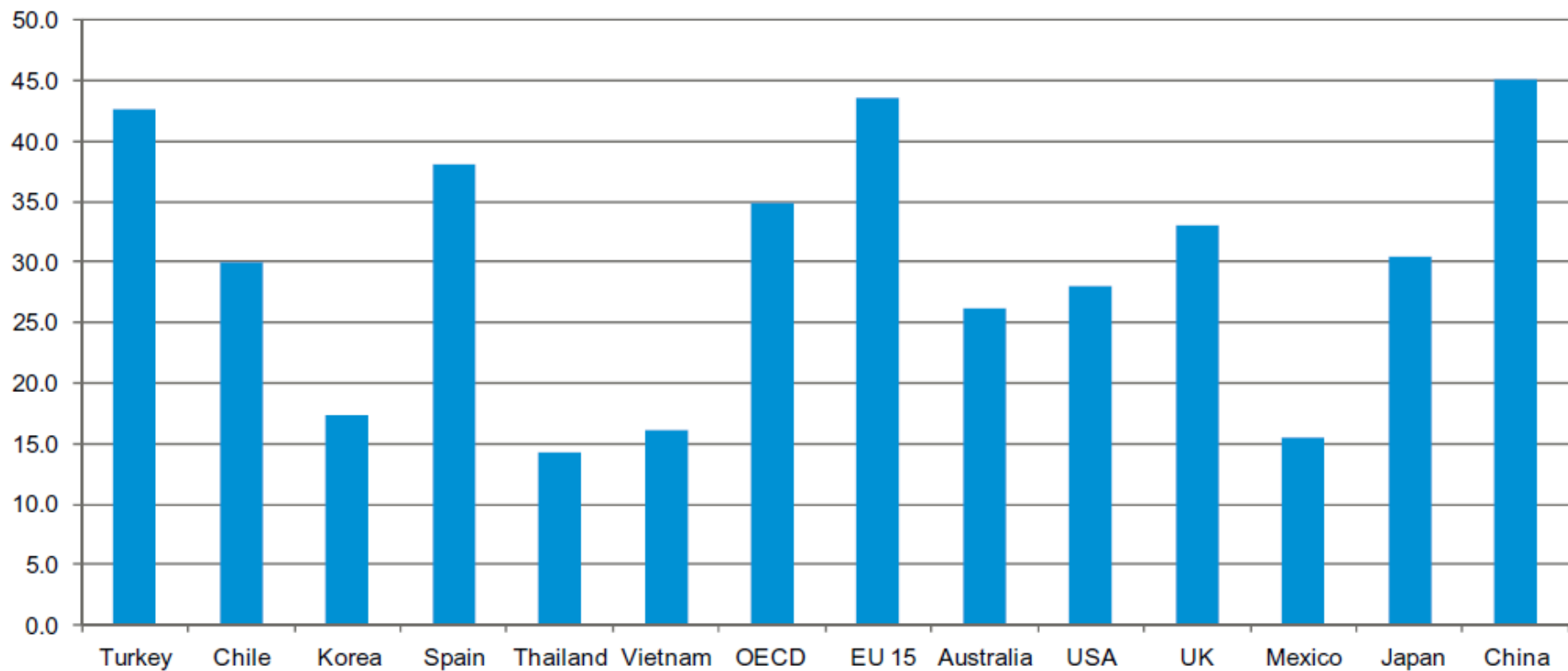


Fig. 5. China's Labor Tax Wedge in Comparative Perspective. Source: OECD (2011). For China, Author Calculation from Aggregate Data.

China's SI programs are decentralized, many benefits NOT portable

Table 4. Pooling Levels of Social Insurance Funds in Urban China.

Urban Population	Outset of Reform	Present	Goal
<i>Urban employees</i>			
Pension insurance	County (2,858)/city or industry	Province (31)	Nationwide (1)
Medical insurance	County (2,858)/city or industry	Prefecture city (333)	Province (31)
Unemployment insurance	Prefecture city (333)	Prefecture city (333)	Province (31)
Work-injury insurance	Prefecture city (333)	Prefecture city (333)	Province (31)
Maternity insurance	County (2,858) or prefecture city (333)	Prefecture city (333)	Province (31)
<i>Urban residents</i>			
Medical insurance	County (2,858) or prefecture city (333)	Prefecture city (333)	Province (31)
Pension insurance	A few cities or prefecture cities	A few cities or prefecture cities	Province (?)

Source: Authors' compilation based on relevant policies, regulations, and laws.

China: Evading High Contribution Rates

- Local Labor Bureaus allow (migrant) workers to opt out of SI programs voluntarily as long as employers offer SI benefits
- SI contributions based on minimum wage or (lower) policy-set wage
- Employer hire workers through labor service companies

Regression results on participation in CI programs (CULS 2005 and 2010)

- Being a rural (urban) migrant in cities reduces the likelihood of participating in CI by 54 (37)%
- Having a labor contract increases participation probability by 27%
- Those in private sector less likely to participate
- One additional year of schooling increases participation probability by 3%
- Age increases participation probability by 3%
- Women are 2% less likely to participate, but effect disappears when controlling for industry and ownership

China Challenges

- Widespread evasion of CI program leads to very low SI coverage of migrant workers
- Rapid expansion of voluntary CI (and NI) programs has been achieved via subsidies but delivers meager benefits
 - Rural pension program has reduced labor supply but increased income and subjective well-being (Giles et al, 2014)
- Large differences in benefits across schemes makes integration of programs difficult
- Greater success of new SI programs not linked to employment creates greater incentives to evade CI programs

Indian Social Insurance Programs (organized sector)

- Employees Provident Fund Organization
 - Provident fund for up to 118 million persons in 393824 establishments as of March 31, 2014
 - Contribution rates: 10-12% workers, 1.67%-3.67% employers
 - Pension scheme for 26 million persons
 - Contribution rates: 0% workers, 8.33% employers, 1.16% government
- Employees State Insurance Company
 - Medical care (and other benefits) for 18.6 million workers, 72.1 million persons
 - Contribution rates: 1.75% workers, 4.75% employers
- Only 35 million of 400 million workers have old-age income protection

Implications for India

- India is challenged by the size of its informal sector, but advantaged by the relative youth of its age structure
- Given complexity and incentive problems associated with multiple programs, moving toward a universal public SI programs have great appeal
 - Only universal systems avoid incentive distortions that lead to misallocation of labor
 - Can reduce burdens on formal sector enterprises and increase competitiveness (Anton, Hernandez, and Levy, 2011)
 - Benefit amounts must be realistic and reflect budget limitations
 - Can be supplemented by employer-provided (voluntary or involuntary) DC programs to support better consumption smoothing