

Chapter 13

Social Protection in China: Current Status and Challenges

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CHAPTER 13

Social Protection in China: Current Status and Challenges

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This paper reviews the current state and challenges of social protection in China. After describing the administrative framework and institutional design of the social protection system in China, the paper mainly analyses the challenges facing social insurance schemes in terms of coverage, pooling and fiscal sustainability. As China is working hard to provide basic social protection for all at present, and many institutional reform measures are being implemented or will be implemented, this paper also summarizes up-to-date practices of the major reforms in improving and perfecting social insurance schemes in China. The paper concludes with some policy suggestions on how to realize the fundamental goal of providing basic protection for all in China.

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1. Introduction

China registered an annual average economic growth rate of 9.8% over the past 30 years, creating a miracle of economic takeoff. Despite the setback of the financial crisis worldwide since 2008, China's economy still experienced rapid growth momentum, with the GDP growth rate in 2009 reaching 8.7% and per capita GDP topping the 3,000 U.S. dollars mark for the first time (NBS, 2010). Currently, China is in a crucial period of economic and social development, and the establishment of a social security system covering urban and rural areas is an important task for this period. However, the special national situation determines that the difficulties and challenges of this task in China are far greater than those in any other country in the world.

China's unique situation is deeply rooted in two unique socio-economic systems: the household register system (the Hukou system) and the land system. These two systems have not only founded the basic economic and social order in China but also created a dual segmentation of China's economic and social systems. Starting from the *Regulations on Hukou Registration of the People's Republic of China* promulgated in 1958, the household register system is a legacy of the planned economy, which was designed mainly to restrict migration from rural to urban areas but later it evolved into a tool of separating the two areas. As various social policies and welfare systems became continuously attached to the household register system, people with urban Hukou and those with rural Hukou received different forms of social protection. China established a social security system for people with urban Hukou, while the rural population had the land, which is thus endowed with the function of guaranteeing their basic livelihood. The rural land system stipulated that land was collectively owned by the rural population but the peasants had rights of land use. This shows that under the planned economy system because of Hukou restrictions on population in urban and rural areas, they could not migrate, and therefore, they received different forms of social protection.

However, market-oriented reforms broke the economic and social order formed under the planned economic system. In urban areas, labor market reform destroyed scores of formal employments; substantial numbers of urban workers, who previously

had better protection under the planned economic system, lost their jobs, and, therefore, urban employment manifested a serious trend of informalization. Before the mid-1990s, there was a high proportion of formal employment in urban areas, and unit employment (approximate to formal employment) had been accounting for about 80% of urban employment. With the accelerating pace of labor market reform, this situation changed rapidly; the proportion of unit employment dropped sharply, and the absolute numbers also showed a decreasing trend. For example, total urban employment was 190.4 million in 1995, of which unit employment was 149.08 million, 78.3% of urban employment. Unit employment reduced to 117.13 million in 2006, only 41.4% of the total. On the other hand the amount and proportion of non-unit employment increased greatly; the number soared from 41.32 million in 1995 to 165.97 million in 2006, while its proportion leapt from around 20% to 58.5%. Non-unit employment increased by 124.65 million during the period from 1995 to 2006, while over the same period total urban employment increased by only 92.7 million; the increment in urban employment was less than that of non-unit employment, which means that not only all of the new jobs created came from urban non-unit employment, but also approximately 30 million people moved from unit employment into non-unit employment (Zhang Juwei, 2009). The informalization of urban employment means that more and more people lack basic social protection.

In rural areas, with the deepening of market-oriented reforms, the binding force of the household register system on population mobility has weakened, resulting in a lot of rural population shifting into urban areas. Without urban Hukou, the floating population cannot join the urban social security system, and thus became an important component of urban informal employment. It is generally estimated that rural population shifting into the urban areas were about 30 million in the mid-1980s, 50 million around the mid-1990s, and 140.41 million in 2008, which means that roughly 1/3 of the rural labor force are working in the urban areas at present (Cai Fang, 2009). On the whole, China's current social security system covers only those urban workers in formal employment, while most of workers, including the rural population, are still lacking basic social protection.

Theoretically, there are two approaches to providing basic social protection for all in China. One choice is to build a uniform social security system to cover all,

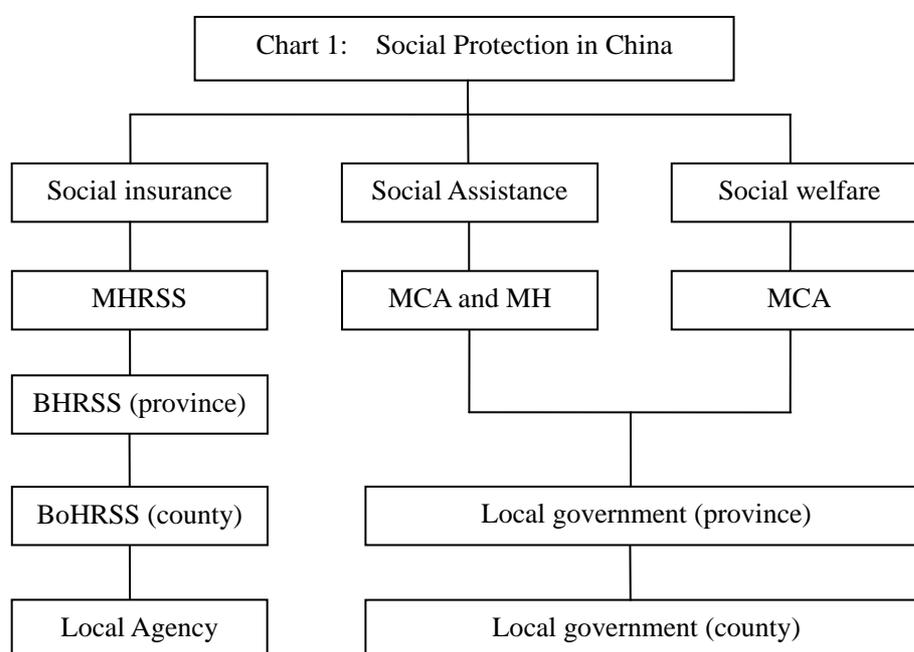
regardless of the rural and urban divide. That is, both rural and urban residents would be covered by the same system of rules. However, under the circumstance that Hukou and land systems still exist and continue to play their roles, the dual economic and social order will not disappear in the short term, so it can only be a “vision” to build such a system, which cannot be turned into reality. The remaining alternative is to set up different social protection systems for urban and rural areas respectively, which is mainly determined by China’s basic national situation (Zhang Juwei & Zhang Shibin, 2010).

2. Current Status of China’s Social Protection

The social protection model formed in China under the planned economy has been broken, and the social protection system adapted to the market economic system is currently under establishment and improvement. So far, the institutional framework of China’s social protection has basically taken shape, and mainly includes three basic systems, namely, a social insurance system, a social assistance system, and a social welfare system. As mentioned earlier, because of China’s large population size, coupled with the huge gap between urban and rural areas, none of the three basic systems is able to cover all people by applying identical rules, but the reality of division between urban and rural areas must continue to be recognized, and thus different treatment must be provided to urban and rural residents. The result is that, unlike most other countries, China cannot establish a social protection system identically applied to urban and rural areas, but must establish one that separately applies to urban and rural areas. Individually, the above-mentioned three basic systems can all be divided into two parts: a rural part and an urban part.

From the viewpoint of public administration, the three basic systems are organized and implemented by different government ministries. The Ministry of Human Resources and Social Security (MoHRSS) is mainly responsible for the social insurance system, including a total of seven insurance schemes: basic pension insurance for urban workers, basic medical insurance for urban workers, medical insurance for urban

residents, new rural pension insurance for peasants, unemployment insurance for urban workers, injury insurance for urban workers and maternity insurance for urban workers. The Ministry of Health (MoH) is mainly responsible for the new rural medical insurance scheme. The Ministry of Civil Affairs (MoCA) is mainly responsible for social assistance and social welfare schemes, including a minimum livelihood guarantee scheme for urban residents, a minimum livelihood guarantee scheme for rural residents, etc. The administrative framework of social protection systems in China is illustrated in Chart 1.



Note: MoHRSS: Ministry of Human Resources and Social Security; BoHRSS: Bureau of Human Resources and Social Security; MoCA: Ministry of Civil Affairs; MoH: Ministry of Health.

2.1. Social Insurance System

The social insurance system includes a total of 8 components, mainly: pension insurance (Old Age insurance), medical insurance, unemployment insurance for urban workers, injury insurance for urban workers, maternity insurance for urban workers, etc. (See Chart 2).

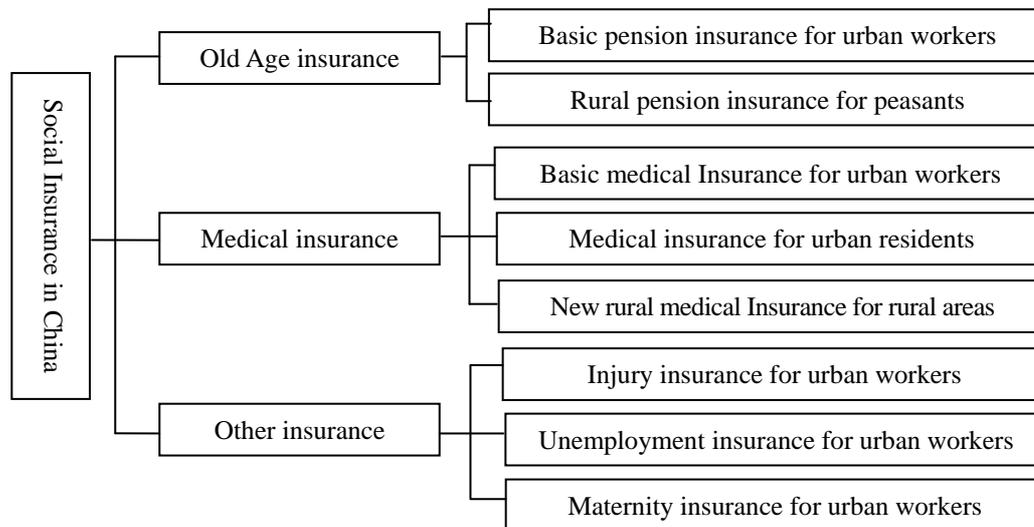


Chart 2: Social Insurance System in China

2.1.1. Pension Insurances

China's pension insurance system is divided into an urban pension insurance scheme and a rural pension insurance scheme, and the urban pension insurance scheme includes two types: one is the basic pension insurance scheme for urban workers and the other is an enterprise annuity scheme.

The basic pension insurance for urban workers is compulsory, i.e., all urban workers must participate in this scheme. Its basic model is a combination of social pooling with individual accounts, and the total contribution rate is 28% of payroll, of which 20% is contributed by the employer and goes into the social pooling account, and 8% is contributed by the employee and goes into the individual's account. Pension benefits are also have two parts, the basic pension allowance and the individual account pension allowance. The former comes from the social pooling account and the latter comes from the individual's account. Workers with accumulated pension contributions of more than 15 years are eligible for basic pension benefits on a monthly basis after retirement and workers with accumulated pension payments of less than 15 years can have a lump-sum payment of their individual accounts (State Council, 1997). A total of 218.91 million people participated in the basic pension insurance scheme for urban workers in 2008, of whom about 53.04 million were receivers of pension, who received

an average pension benefit about 1,100 Yuan per month, representing a replacement rate of 50% (pension benefit as a percentage of average wage before retirement) (NBS, 2009). The total income of the pension fund in 2008 was 974 billion Yuan, of which 801.6 billion came from contributions and 143.7 billion came from financial subsidies by all levels of government; the total expenditure was 739 billion Yuan and the accumulated year-end balance of the basic pension insurance fund was 993.1 billion Yuan (NBS, 2009).

The term “Enterprise Annuity” refers to a supplementary pension insurance scheme established by enterprises for employees in accordance with their economic strengths and implemented under national policy provisions and conditions, which is subject to national macro-guidance and to the internal decision-making of the enterprises. 33,000 Chinese enterprises had established enterprise annuity schemes by the end of 2008, with the number of participating workers at 10.38 million and the year-end balance of enterprise annuity funds at 191.1 billion Yuan. All the capital was managed by investment management companies and asset custodian companies that met relevant qualifications. Although the enterprise annuity system is developing rapidly, there are some problems. First of all, though the number of enterprises establishing annuity system increased rapidly, i.e. from 24,000 in 2006 to 33,000 in 2008, the increase in the number of people covered by the system did not significantly increase (from 9.64 million to 10.38 million in the corresponding period (NBS, 2009)). Second, the development of the enterprise annuity scheme is highly unbalanced; 90% of the enterprise annuity funds were accumulated from large state-owned enterprises, which are in industries with advanced economic performance, such as coal, electricity, petrochemicals and telecommunications industries, while small- and medium-sized enterprises which account for 99% of the total have accumulated less than 10% of the total enterprise annuity funds. The enterprise annuity system is actually widening income inequality among industries, among enterprises, as well as among different positions within enterprises. In addition, as relevant policies stipulate that in enterprises where an annuity scheme has been set up, 4% of the payroll can be deducted before tax, directly offsetting taxable income, the enterprise annuity system has thus been suspected of being a tool of tax avoidance in some of the enterprises.

In rural areas, people traditionally rely on family and land for security in old-age

and the social insurance system has been absent for a long time. China began to carry out a new pilot project of rural pension insurance for peasants in 10% of the counties (cities, districts) across the country as late as in 2009. The new rural pension insurance for peasants adopts a model that is a combination of social pooling with individual accounts and is designed to cover all rural residents from 16-60 years of age (non school students, peasants who do not participate in the basic pension insurance for urban workers). Its funds are raised by a model combining individual contribution, collective assistance and government subsidies, in which individual contribution can be classified into five levels, namely 100 Yuan / 200 Yuan / 300 Yuan / 400 Yuan / 500 Yuan per year. The value of pensions issued every month is one 139th of the total value in a retiree's account. The government pays the full amount of basic pension allowance for peasants who are eligible for withdrawal and central government grants the full amount of subsidies for central and western regions and 50% of subsidies for the eastern region according to pension standards. The basic pension standard was 55 Yuan per person per month in 2009 (State Council, 2009a). At present, this system is still at the pilot stage.

2.1.2. *Medical Insurance*

For different types of people, China has established three kinds of medical insurance systems: basic medical insurance for urban workers, basic medical insurance for urban residents and a new rural cooperative medical insurance.

The basic medical insurance for urban workers is designed to cover urban employees. The employer and employee respectively contribute 6% and 2% of the wages and a model of combining pooled funds with individual accounts has been adopted. As for the requirements of payment, it is stipulated that the pooling fund pays medical spending when it is above the bottom line of payment, equivalent to 10% of average annual wage and that below the cap of payment equivalent to 4 times of the average annual wages while individual insurer needs to share a co-payment of 20% the spending. When the medical spending is below the bottom line payment, it will be totally paid by the individual account or by the insurers themselves (State Council, 1998).

The basic medical insurance for urban residents covers: primary and secondary

school students (including vocational high school, intermediary professional school and technical school students), teenagers and children, and other urban residents who are not employed and therefore are not covered by the basic medical insurance system for urban workers. The funds for the basic medical insurance for urban residents is collected from the contributions of insured people and from governmental subsidies, while giving special assistance to vulnerable groups. At present, the standard government subsidy is about 120 Yuan per person per year and it is managed in the same way as the basic medical insurance for urban workers. The basic medical insurance fund for urban residents is principally used for in-hospital and serious illness expenses of the insured people and the current reimbursement rate is around 60% of the total expense; some localities are gradually integrating outpatient medical costs on a pilot basis. The basic medical insurance scheme for urban residents started its national pilot in 2007 and 118.26 million urban residents had participated in the scheme by the end of 2008; university students were included into the scheme in 2009, pushing the number of people covered by the scheme to more than 150 million (MoHRSS and NBS, 2009).

In rural areas, the Chinese government initiated the new rural cooperative medical scheme (shortened as the “new rural cooperative”) in 2003. The “new rural cooperative” is characterized by diversified sources of funding; through the main source, which is individual contributions and other sources like collective support and government subsidies, mutual assistance among peasants for “serious illness pooling” is being achieved. The new rural cooperative medical system covers all peasants and uses a funding mechanism combining individual contributions, collective support and governmental subsidies; current individual contribution fee is about 40-80 Yuan per person per year, government subsidy is 120 Yuan (Wen Jiabao, 2010) and the pooling is mainly done at the county (city) and township level. The rural cooperative medical system mainly pays for large medical expenses or in-hospital medical costs of the peasants who participate in the scheme with a current average reimbursement rate of 60% of the total expense. Up to the present, all county-level regions have already started implementing the new rural cooperative medical scheme and have achieved their target of full coverage.

2.1.3. Other Social Insurance Schemes

Unemployment insurance for urban workers is designed to cover urban workers in urban state-owned and collective enterprises, foreign-invested enterprises, urban private enterprises and other urban enterprises; the enterprise and the employee pay respectively 2% and 1% of the wages as unemployment insurance premiums and currently these contributions are mainly pooled at the county level. Unemployment insurance allowance is paid monthly; the standard and period are determined according to the duration of premium contribution. The benefit of unemployment insurance can last for 24 months and the allowance is lower than local minimum wage but higher than the urban minimum livelihood guarantee level (State Council, 1999).

Injury insurance for urban workers covers workers in all types of enterprises and hired workers in small industrial and commercial firms; all the injury insurance contributions are paid by the employer, and different contribution rates, ranging from 0.5% to 2.5% of the payroll, are applied to different industries based on the degree of risk. Payment by injury insurance includes: the cost of treatment of injuries, payroll, living allowance and some medical care costs during the period of treatment; the maximum period of benefit should not exceed 12 months (State Council, 2003).

Maternity insurance for urban workers covers women workers in government departments, public organizations, institutions and enterprises; insurance contributions are paid by the employer, at a rate between 0.5% - 1%, while individual workers do not need to pay and funds are currently pooled at the county level. Payment by the maternity insurance scheme includes: allowances during the period of maternity leave according to the average monthly wage of workers in the company in the previous year, women workers' examination fees, delivery fees, surgery fees, in-hospital fees and drug fees and medical expenses incurred women workers by illness following childbirth.

2.2. Social Assistance

China has accomplished the transformation from a traditional social relief system to a modern social assistance system and has preliminarily established a social assistance system with the following as its main contents: a minimum livelihood guarantee system in urban and rural areas, a five-guarantee scheme (a type of welfare scheme for widowed, disabled and orphans in rural areas, which provides those people with basic

livelihood and expense of their funeral) in rural areas, medical assistance systems in urban and rural areas, educational assistance, housing support, legal assistance and a relief system after natural disasters.

The minimum livelihood guarantee scheme for urban residents covers urban residents with non-agricultural Hukou, whose per capita income is lower than the local urban minimum living standard. Local governments integrate the minimum livelihood guarantee fund into government budgets and the civil affairs departments of local governments above the county level are responsible for this scheme. A total of 23.34 million urban residents were covered by the minimum living guarantee in China in 2008 with an average guarantee level of 205 Yuan, which is equivalent to 15.6% of the average disposable income of urban residents (Wu Hongxin *et al.*, 2009).

The minimum livelihood guarantee scheme for rural residents covers all rural households whose per capita annual net income is below the local minimum living standard. Funding for the rural minimum livelihood guarantee scheme comes from local governmental budgets and central government grants appropriate subsidies to poor regions. Nearly 43 million people were covered by the rural “minimum livelihood guarantee” as of the end of 2008 with an average level of 82 Yuan per capita per month, which is equivalent to 20.7% of peasants’ per capita net income (Wu Hongxin, *et al.*, 2009).

Medical assistance covers families in rural areas suffering from serious illness affecting their basic livelihood, whose individual medical expenses are still unaffordable, even after accepting cooperative medical insurance. Medical assistance funding comes from government budgets and is managed by the local civil affairs departments. Medical assistance in rural areas was made available as many as 936 million times in 2008 (NBS, 2009). Urban medical assistance covers urban family members suffering from serious illnesses which affect their basic livelihood, and the assistance method combines direct relief aid payments with waiver of some medical costs.

2.3. Social Welfare

China has strengthened its legislation on social welfare and has successively passed the “*Law on Protection of Disabled Persons*”, “*Law on the Protection of Women’s Rights*”, “*Law on Protection of the Rights and Interests of the Aged*” as well as the

“Welfare Donations Law” since 1990. By the end of 2008, there were about 2.35 million beds in various welfare institutions available for accommodation of helpless people and there are about 1.89 million of such people were actually accommodated; in cities and towns, some 109,000 community service facilities and 9,871 community centers have been established; annual sales of social welfare lottery tickets were 60.4 billion Yuan, raising public welfare funds of 21.1 billion; social donations of 48.2 billion Yuan were directly received. In 2008, the people covered by the five-guarantee scheme enjoyed governmental subsidy of 2,176 Yuan for those who were centrally supported and 1,624 Yuan for those who were supported individually (NBS, 2009).

3. Challenges Facing China’s Social Protection

China continues to accelerate the construction of its social protection system for all and a number of schemes have been introduced in recent years. However, in general the coverage of social insurances is still low and the challenges are severe.

3.1. China’s Population is Aging Rapidly but Most People are still not Covered by Any Pension Insurance

The huge population is China’s basic national reality. With a total population of 1.33 billion and an urbanization rate of around 46%, more than half of the population was still living in rural areas in 2008. At present, 110 million people are above 65 years of age, accounting for 8.3% of the total population and this proportion will soar to 26.2% in 2050; such a pace of aging is rare in the world (Table 3.1). What’s more, the shifting of rural working-age population to urban areas has greatly changed the distribution in age structure of urban and rural populations, so that the degree of aging in rural areas is much more obvious than in urban areas, and therefore, the rural areas face a more severe aging situation than urban areas.

Table 3.1. Population Projection in China: 2010-2050

Year	Total population (10 thousand)	Working age population 16-64 years (10 thousand)	The aged population 65 or above (10 thousand)	Degree of aging (%)	Support ratio
2010	133555	96961	11460	8.58	8.46
2020	139206	98708	17146	12.32	5.76
2025	140272	97757	19968	14.24	4.90
2030	139769	95335	23874	17.08	3.99
2035	138366	90730	28989	20.95	3.13
2040	136426	86048	32788	24.03	2.62
2045	133575	82573	33708	25.24	2.45
2050	129320	78668	33871	26.19	2.32

Source: Institute of Population and Labor Economics, Chinese Academy of Social Sciences.

The aging of China's population will lead to a decrease in the social support ratio, creating a labor burden as well as a cost. China's supporting ratio (the number of working age population divided by the number of the aged at 65 or above) was 9.81 in 2000 and will drop to 2.32 in 2050 but in sharp contrast to this, the pension insurance coverage is quite low (Table 3.2) and the vast majority of people still have not been covered by any form of pension insurance system.

In urban areas, since the mid-1990s, the Chinese government has continued to accelerate the construction of basic pension insurance for urban workers, vigorously expanded its coverage and the number of people covered has increased from 110 million in 1995 to 220 million in 2008. However, due to the growth of the urban working-age population in the same period, the rise in the coverage ratio of basic pension insurance for urban workers is not obvious. Though the proportion of people covered by that insurance compared to the urban working population has surged from about 46% in 1995 to 55% in 2008, yet from the perspective of the proportion of people covered by that insurance among the urban working-age population it has only increased from 40.6% in 1995 to 43% in 2008.

Table 3.2. Coverage of Basic Pension Insurance for Urban Areas

Year	Urban population above 16 years	Number of Employed workers	Total number of insured persons	Number of insured working persons	Coverage ratio for the employed persons	Coverage ratio for the working population above 16
1995	27062	19093	10979	8738	45.8	40.6
2000	38561	23151	13617	10447	45.1	35.3
2001	38453	23940	14183	10802	45.1	36.9
2002	40426	24780	14737	11129	44.9	36.5
2003	42707	25639	15507	11647	45.4	36.3
2004	44125	26476	16353	12250	46.3	37.1
2005	45939	27331	17488	13120	48.0	38.1
2006	48109	28310	18766	14131	49.9	39.0
2007	49504	29350	20137	15183	51.7	40.7
2008	50922	30210	21891	16588	54.9	43.0

Source: Based on relevant statistical data in *China Statistical Yearbook* in various years.

Note :Unit in ten thousand persons and percent

In rural areas, most people still have not been covered by any social pension insurance scheme (Table 3.3). China began to introduce a social pension insurance plan in the rural areas in the mid-1980s but because the government did not share necessary responsibility in the early period, coverage had stalled at around 10% for a long time, and, especially, the insured number declined after 1999. China began to establish a new social insurance scheme in 10% of the rural areas that were selected as pilot areas in 2009 hoping that the system will cover more of the rural population in the near future.

Table 3.3. Coverage of Rural Pension Insurance and Total Coverage for Rural and Urban as a whole.

Year	Urban population above 16 years	Total number of insured population	Coverage ratio for rural working age population	Total coverage ratio for rural and urban as a whole
1995	60210	5143	8.5	18.5
2000	57141	6172	10.8	20.7
2001	58173	5995	10.3	20.9
2002	58033	5462	9.4	20.5
2003	57182	5428	9.5	21
2004	57292	5382	9.4	21.4
2005	56595	5442	9.6	22.4
2006	53834	5374	10	23.7
2007	53966	5172	9.6	24.5
2008	53774	5595	10.4	26.3

Source : Institute of Population and Labor Economics, Chinese Academy of Social Sciences.

Note : Unit in ten thousand persons and percent

To sum up, it can be seen that, compared with the situation of rapid aging, China's pension insurance system lags far behind. If the populations covered by urban and rural social pension insurance are added together, the coverage ratio would just surpass 1/4, which means that about 3/4 of the population above the age of 16 are not covered by any pension scheme. This is currently one of the most serious social challenges for China; how to expand pension insurance coverage so that more people are covered by the pension insurance system.

3.2. The Level of Pooling is Low and the Different Benefits in Different Pools are Creating more Inequality

China's social insurance system is not only divided between urban and rural areas but also has too low a level of pooling, with the result that the system is often divided into thousands of pooling units. Social insurance policies are often determined by different departments according to different objectives to meet different needs at different times, while most are implemented separately, and the linkage of various policies is less considered. Different regions have different levels of social insurance contribution and there are a variety of levels of income and expenditure even within the same province, resulting in different forms of social security for the population with

different Hukou statuses and with a varied nature of jobs.

Of course, the low-level social insurance pooling is rooted in the imbalance of China's inter-regional economic and social development, which also is still further expanding (Table 3.4). From the perspective of income level, the national per capita income ratio between urban and rural areas jumped from 2.57:1 in 1978 up to 3.35:1 in 2008; in terms of per capita GDP, that of Shanghai was 8.2 times that of Guizhou, while Guangdong and Jiangsu provinces are 4.2 times that of Guizhou in 2008.

Table 3.4. Economic and Social Development of Urban and Rural Areas in Different Regions in 2008

Region	Per capita GDP (Yuan)	Per capita income of urban areas (Yuan)	Per capita income of rural areas (Yuan)
Beijing	63029	24725	10747
Shanghai	72553	26675	11385
Jiangsu	39083	18680	7357
Guangdong	37588	19733	6400
Guizhou	8824	11759	2797
Gansu	12110	10969	2725
Qinghai	17365	11648	3061
Ningxia	17892	12932	3681
Ratio of the highest over the lowest	8.2	2.4	4.2

Source: Statistical Communiqués issued by The Central Government and different regions in 2008.

The tremendous differences in economic and social development between urban and rural areas and among regions forced China to implement its social insurance plans at lower pooling levels (Table 3.5). Prior to the 1990s, China's urban pension insurance basically relied on enterprise pooling and even until now has not yet fully achieved provincial pooling. County-level pooling has been implemented in rural pension insurance, which means that China has more than 2,000 pooling units and the inter-regional contribution level and wage level are difficult to unify, leading to the "fragmentation" of the social insurance system. After years of development, each pooling level has formed its own unique interests and become an obstacle to pooling level elevation.

Table 3.5. Pooling Levels of Pension and Medical Insurance in China's Urban and Rural Areas in Different Periods

Period	Urban pension insurance	Rural pension insurance	Urban medical insurance	Rural medical insurance
From 1949 to the end of 1980s	Pooling at enterprise level	Village	Pooling at enterprise level	Village
From early 1990s to early this century	Pooling at city, county and industry level	County, city	Pooling at city, county and industry level	Township
Currently	Pooling at provincial level in most provinces	County, city	Pooling at city level	Township

Source: Compiled based on relevant governmental documents materials.

Pooling at a lower level will inevitably lead to greater differences in social insurance benefits among different groups. Take the pension insurance system as an example; the benefit of rural pension insurance for peasants is less than one-tenth of the basic pension insurance for urban workers, and is only equivalent to the minimum livelihood guarantee level in rural areas (Table 3.6).

Table 3.6. Average Monthly Pension Benefits by Urban and Rural Pensioners

Year	Average monthly pension of rural pensioners	Average monthly pension of urban pensioners	Ratio of rural pension to urban pension for workers	Ratio of rural per capita income to urban per capita income
2000	34	559	0.06	0.36
2001	39	576	0.07	0.34
2002	35	648	0.05	0.32
2003	61	674	0.09	0.31
2004	38	705	0.05	0.31
2005	56	758	0.07	0.31
2006	68	873	0.08	0.31
2007	82	1002	0.08	0.30
2008	90	1100	0.08	0.30

Source: The pensions under urban pooling are drawn from the *China Labor and Social Security Yearbook*; the rural pensions are calculated according to data from the *China Labor and Social Security Yearbook*; the urban and rural per capita income and their ratios are calculated according to data from the *China Statistical Yearbook*.

Note: Unit in Yuan / person, month

In urban areas, the average pensions for retirees from business enterprises are significantly lower than those of administrative departments and public institutions, at

only around 60% of the administrative departments' level (Steven Dunaway and Vivek Arora, 2007). In contrast, the ratio of enterprise workers' wages to those of administrative department workers' is about 0.9:1 or approximately equal. Therefore, the existing basic pension insurance scheme for urban workers has expanded the lifetime labor income inequality between enterprises and government organizations, and the pension insurance scheme has become a source of inequality (Table 3.7).

Table 3.7. Average Monthly Retirement Payments in Different Pools

Year	Enterprises	Administrative departments	Public institutions	Ratio of pension between enterprises and administrative departments	Ratio of average payroll between enterprises and administrative departments
2000	544	947	871	0.57	0.92
2001	556	940	894	0.59	0.86
2002	618	1077	1031	0.57	0.85
2003	640	1124	1091	0.57	0.86
2004	667	1223	1154	0.55	0.87
2005	719	1257	1208	0.57	0.86
2006	835	1364	1290	0.61	0.88
2007	947	1717	1576	0.55	0.84

Source : China Statistical Yearbook in various years.

Unit : in Yuan/ person, month

3.3. The 'Holes' in the Social Insurance System exclude Migrant Workers from the Protection of Social Insurance System

In theory, the on-going system of social insurance is still able to achieve universal coverage even with a separation of the system between rural and urban areas. However, the reality is that China's rapid urbanization and industrialization have led to a large number of people migrating in a constant flow from rural to urban areas. These people are difficult to incorporate into a suitable social insurance scheme. Without urban Hukou, the migrants can hardly participate in the urban social security scheme and even despite their accession to it, they will not only face the problem of dealing with the issue of rural land income but also the risk that on returning to the rural areas, they will be unable to receive off-site social security benefits. Meanwhile, though these migrants

have rural Hukou and land, in fact, they have become “urban people” and many are not likely to return to rural life in the future, so joining a rural social insurance system is not particularly meaningful to them.

This is exactly the reality. The size of China’s rural migrant labor force reached 140.41 million in 2008 but the proportion of their participation in urban social insurance schemes is quite low (Table 3.8). The main focuses of such participation as they achieve are medical insurance and injury insurance for urban workers. In the same year, about 30.3% of rural migrant workers joined schemes for medical insurance for urban workers and approximately 35.4% of rural migrant workers joined schemes for injury insurance for urban workers but the proportion of participation in basic pension insurance schemes for urban workers was only 17.2%, less than half of injury insurance coverage ratio (MoHRSS and NBS, 2007, 2008). Owing to factors such as the difficulty of inter-regional transfer of pension insurance and the need for 15-years’ accumulated contributions before receipt of post-retirement pension, the rate of insurance surrender of by rural migrant workers is very high; for instance, persons without Shenzhen Hukou have had access to pension insurance since 1987 but only about 100 people can truly enjoy the pension 15 years later. As a result, the pension insurance surrender rate of rural migrant workers reached 40% in eastern coastal areas and rural migrant workers always wait to surrender insurance in droves every New Year’s eve before returning home (Zhang Meng, 2009).

Table 3.8. Participation by Rural Migrant Workers in Social Insurance

Year	Number of rural migrant workers	Pension insurance		Medical insurance		Injury insurance for urban workers	
		Number of participants	Coverage ratio	Number of participants	Coverage ratio	Number of participants	Coverage ratio
2006	11891	1417	11.9	2367	19.9	2537	21.3
2007	12609	1846	14.6	3131	24.8	3966	31.5
2008	14041	2416	17.2	4249	30.3	4976	35.4

Source: Calculated based on *Statistical Communiqué on China’s Human Resources and Social Security Cause*.

3.4. The Nominal Social Insurance Contribution Rates are Too High and Contribution Evasion is a Serious Problem

Social insurance evasion is a common problem faced by developing countries. China is no exception. In China, if various social insurance contributions were all paid, the total contribution would amount to 39-42.5% of the payroll. Under the circumstance of high contribution, some employers, especially private companies, work out every possible way to evade contribution, leading to a rather high contribution evasion rate for social insurance; this proportion generally exceeded 60% before 2001. In recent years, due to gradual improvement of the contribution collection system, contribution evasion has significantly decreased, but even so, evasion still amounted to 27% in 2008 (see table 3.9).

Table 3.9. Contributions and Evasion of China's Social Insurance

Year	Nominal Social Insurance revenue	Real Contribution revenue	Total Evasion	Evasion rate
2001	4734	2696	2038	43.1
2002	5373	3581	1791	33.3
2003	6131	4332	1799	29.3
2004	7136	5142	1995	28.0
2005	8479	6306	2173	25.6
2006	10116	7661	2455	24.3
2007	12396	9619	2776	22.4
2008	15531	12209	3322	21.4

Source: Calculated based on *China Statistical Yearbook* in various years.

The high contribution rate is an important reason why rural migrant workers are unable to participate in the urban social insurance system. The social insurance contribution level for urban workers is calculated based on average wages, and the floor limit of the payment is 60% of the average wage and the cap is 300% of the average wage (Zhang Hongtao and Kong Jingyuan, 2008). The high contribution rates and low wages of rural migrant workers resulted in the consequence that their actual social insurance contribution rate is higher than their nominal rate (Table 3.10). In theory, if rural migrant workers all join all the urban social insurance schemes, the total contribution rate would be around 41% of their wages. However, as the average wages of rural migrant workers are generally less than 60% of the social average wage, the

actual social insurance contribution rate of rural migrant workers is obviously higher than the nominal contribution rate; for example, in 2007 the contribution of rural migrant workers involved in social insurance for urban workers was equivalent to 50% of their total average wage, far higher than the nominal contribution rate of 41%.

Table 3.10. Actual Contribution Rates by Rural Migrant Workers to Social Insurance for Urban Workers under the Current System

Year	Social average payroll	Average payroll of rural migrant workers	Proportion of rural migrant workers' payroll in social average payroll	Contribution standard of social insurance	Ratio between social insurance contribution and payroll of rural migrant workers
2003	14040	8424	60	3454	41
2004	16024	9360	58	3942	42
2005	18364	10332	56	4518	44
2006	21001	11352	54	5166	46
2007	24932	12180	49	6133	50
2008	29229	16800	57	7190	43

Note: China's current social average payroll is calculated according to the average payroll of workers in cities and towns and does not include rural migrant workers and the self-employed. It is assumed that the total social insurance contribution rate is 41% and employers pay 30% of the total employees' payroll as social insurance contributions.

4. Current Major Reforms

In order to expand the coverage of the social insurance system, China has speeded up the construction and reform of the social insurance system. The *Social Insurance Law (Draft)*, which is currently under third examination by the National People's Congress, has embodied the direction and practices of social insurance reforms and is expected to resolve many of the current problems after its passage. In summary, current reforms of social insurance system are mainly concentrated on the following aspects: first, improvement of the social insurance system and expansion of its coverage; secondly, elevation of the level of pooling and achievement of inter-regional pension insurance transfer; thirdly, standardization in the income, expenditure and management of social insurance funds.

4.1. Increasing Coverage of Social Insurance is a High Priority

In order to expand the coverage of social insurance schemes, the current main approach is to constantly strive to establish and improve the system. Expansion of the coverage of social insurance schemes has been made a key indicator of economic and social development in China's "Eleventh Five-Year Plan" to, and it has been set as a target that during the Eleventh Five-Year period, more than 10 million people per year should be added to the basic pension insurance scheme for urban workers and that the total should exceed 220 million at the end of the planning period. The *Guidance Opinions on Launching Pilot Work of New Rural Pension Insurance by the State Council* in 2009 clarified that, all peasants above 16 years of age (excluding school students) who do not join the basic pension insurance scheme for urban workers will be included into the rural pension insurance scheme for peasants, and proposed that before 2020 the system must achieve full coverage; to realize this goal, the central government will provide a basic pension of 55 Yuan per capita per month (State Council, 2009a).

Views on Solving the Issue of Rural Migrant Workers by the State Council in 2005 required that priority should be given to solving the problems of rural migrant workers' injury insurance and serious illness insurance and that pension insurance issues also should be gradually solved. The *Labor Contract Law* promulgated in 2007 stipulates that employers should establish labor relations with workers from the date of employment and must sign labor contracts with the workers, in which social insurance and labor protection should be included (NPC, 2007). *Social Insurance Law (Draft)* provides in legal form that urban workers should join the basic pension insurance scheme and that employers and employees should jointly pay contributions; small industrial and commercial businesses without employees and part-time employees are also eligible to join the basic pension insurance scheme, paying their own contributions (NPC, 2008).

The new rural cooperative medical insurance scheme began to be established by all levels of government in 2003 and it covered 833 million peasants in 2009, with a coverage rate of 94%; the medical insurance system for urban residents began to be established in 2007 and university students were integrated into the system in 2008; more than 150 million urban residents had joined the medical insurance system for urban residents by 2009. *Reform Plan for Deepening Medical and Health System* in

2009 clearly indicates that by 2011, a comprehensive coverage of the basic medical insurance system for urban and rural residents should be realized and that participation rates in basic medical insurance schemes for urban workers and the new rural cooperative medical insurance for rural residents should exceed 90% (State Council, 2007, 2009a; 2009b; 2009c).

4.2. Increasing Pooling Levels and Making Social Insurance Portable when Workers Move from One Place to Another

For a long time, China's various social insurances have been pooled at the county or city level, with the result that one insurance system is often split in thousands of pooling units, which has seriously hampered the development of the various social insurance schemes. The central government has always been committed to elevating the level of pooling but the lack of effective legal means has made such efforts ineffective. The *Social Insurance Law (Draft)* clearly lays down that the basic pension insurance scheme should be pooled at the provincial level and can be pooled at the country level when conditions are ripe; the time and steps for the pooling of other social insurance funds at the provincial level should be provided by the State Council. These articles of the *Social Insurance Law (Draft)* will undoubtedly provide a strong legal basis for elevating the pooling levels of social insurance, and when the law is passed, it will greatly promote the development of the various social insurance schemes.

To elevate the pooling level will be very helpful in the resolution of inter-regional pension insurance transfer issues. The *Social Insurance Law (Draft)* provides that when an employee pursues inter-regional employment, the basic pension insurance should be transferred with the employee, and on retirement, the basic pension should be calculated in accordance with the standards and period and places where contributions are paid and can be paid at the place of retirement. To this end, the State Council promulgated the *Interim Measures on the Transfer and Continuation of Basic Pension Insurance for Urban Enterprise Workers* at the end of 2009, which stipulates that from 2010 onwards, the insured employees, when transferring the basic pension insurance on an inter-provincial basis, they can transfer 12% of the money from the pooling account coupled with the total amount of the money from the individual account (State Council, 2009d). Meanwhile, the State Council also promulgated the *Interim Measures on the*

Transfer and Continuation of Basic Medical Insurance of Rural migrant workers at the end of 2009 (State Council, 2009e).

4.3. Better Management of Social Insurance Funds

It is known that the income, expenditure and management of social insurance funds in China are not up standard and often lead to scandals involving embezzlement of funds. To correct this, the *Social Insurance Law (Draft)* clearly defined the income, expenditure and management of social insurance funds. With regard to insurance contributions, the government has established a unified national individual social security number by using the identification number of every citizen. Employers must, within thirty days from the commencement of employment, apply for social insurance registration for employees to the social insurance institutions and pay social insurance contributions on behalf of the employees; small industrial and commercial firms or businesses without employees, and part-time workers, can apply directly to the social insurance institutions. In terms of administration and operations, the social insurance funds are administered in different accounts and managed by split accounting in accordance with the respective social security insurance; they should not overlap with or be transferred to each other and funds are earmarked; the funds can preserve value through investment and operations aimed at security, in accordance with the relevant provisions of the State Council. Governments above the county level must establish social insurance fund budgets according to the pooling level, achieve balance for social insurance funds and provide assistance when the social insurance funds develop deficits.

5. Suggestions

To some extent, the current reform measures will solve the problems of the social insurance systems' troubled development but cannot be an elixir for all problems. To the underlying problems of further expanding the coverage of social insurance, and in particular, settling the migrant population's participation in social insurance still require long-term hard work. In the long run, it is necessary to consider and cope with the following two issues for further reform of social insurance system.

5.1. Establishing a Social Insurance System with National Pooling

Important issues of social insurance are related to the low level of pooling; the implementation of provincial-level pooling will substantially mitigate the extent of the issues but will not fundamentally solve them. As inter-provincial transfer of social insurance is actually an adjustment of, and competition for, rights and responsibilities in respect of social insurance among the provinces, involving the distribution of benefits, it has an impact on the interests of both receiving regions and sending regions, and the problems cannot be solved under the current design of the system. Therefore, in the long run, establishing a social insurance system with national pooling is the fundamental way to solve the problem, which means that the central government will assume greater responsibility and give more financial input in the provision of social insurance services. At present, local governments are primarily responsible for China's social security system, while the central government has less responsibility and the social security expenditures of central government have been below 10 per cent of total social security expenditures, with a declining trend. The main reason lies in the fact that each social insurance scheme is based on local pooling. With the gradually enhanced fiscal strength of central government, it is possible for the central government to take on more responsibility and to implement a basic social insurance system with national pooling.

5.2. Accelerate the Reform of Houkou System and Explore an Effective way to Include Migrant Workers in the Social Insurance Schemes

Bringing migrants into the social insurance system has always been a crucial issue in expanding the coverage of social insurance. However, so far, there is still no effective approach to solving this problem. It is true that inter-regional transfers of pension insurance for urban workers and medical insurance for urban workers, introduced in 2009 would, to a certain extent, enable a “floating” population in cities and towns to actively participate in basic social insurance but this cannot fundamentally unravel the problem of migrants' insurance participation. Because of low income, unstable employment and short careers, migrant workers will face many difficulties and risks when joining the urban basic social insurance scheme. First, the over-high contribution rate of the urban basic social insurance scheme is unbearable for rural

migrant workers with low income levels. Secondly, in accordance with the current transfer approach, rural migrant workers can only draw the funds from their individual account and part of their pooling account, so social insurance rights have not been fully protected, and furthermore, they face a big risk in the loss of pension benefits if conditions cannot be met at the time of retirement. In the long run, in order to expand social insurance coverage, we must accelerate the reform of the household register system and eliminate the different treatment for people with different Hukou status. Specifically, rural migrant workers should be brought under management in cities and towns; just as the population with urban Hukou, they should enjoy the same public services and resources; some of the agricultural migrant population who meet relevant conditions should be allowed to pursue employment and settlement in urban areas; Hukou restrictions in medium- and small-sized cities and towns should be relaxed so that rural migrant workers can enjoy stable employment and life in cities and towns.

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