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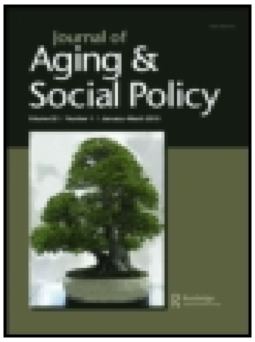

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Pension Reform in China

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Abstract

This article analyses China's pension arrangement and notes that China has recently established a universal non-contributory pension plan covering urban non-employed workers and all rural residents, combined with the pension plan covering urban employees already in place. Further, in the latest reform, China has discontinued the special pension plan for civil servants and integrated this privileged welfare class into the urban old-age pension insurance program. With these steps, China has achieved a degree of universalism and integration of its pension arrangement unprecedented in the non-Western world. Despite this radical pension transformation strategy, we argue that the current Chinese pension arrangement represents a case of 'incomplete' universalism. First, its benefit level is low. Moreover, the benefit level varies from region to region. Finally, universalism in rural China has been undermined due to the existence of the 'policy bundle'. Additionally, we argue that the 2015 pension reform has created a situation in which the stratification of Chinese pension arrangements has been 'flattened', even though it remains stratified to some extent.

Keywords: aging society, China, old-age pension, stratification, universalism

1 Introduction

In 2000, the number of people aged 60 and over reached 10 percent of the total Chinese population, making China an ageing society according to internationally recognised standards (Benbo, 2002). China is widely recognised as a nation that is ‘growing old before getting rich’ (Frazier, 2013; Booth, 2013).

China has undergone a significant and rapid demographic transformation, which has led to an increasingly top-heavy population pyramid, i.e. percentage of elderly people versus working-age population. Therefore, a comprehensive social protection system for the elderly provided by the government has become one of the most pressing concerns for the country with the largest elderly population in the world (Liu & Sun, 2014). In this article, we shed light on recent developments in China’s pension arrangement, since this issue has been little researched as yet, particularly within international academia. Beyond providing an introduction to pension reform, we also explore and analyse the institutional transition of the Chinese pension arrangement.

It is encouraging to find that recently China has established a universal non-contributory pension covering urban non-employed workers and rural residents, combined with an old-age insurance program covering urban employees. The new target of this social pension scheme is the full coverage of all Chinese citizens via a widening social safety net. Despite a strong tendency toward universalism, the current Chinese pension arrangement embodies a fragmentary nature. Various social groups, including rural residents, urban non-employed residents, and urban employees, enjoy different pension benefits, which results in the stratification of social welfare. However, we find pension stratification has been flattened significantly in recent years. For example, in January 2015, the pension program for civil servants and public sector employees was abolished, and they are now subject to the same pension rules as employees in enterprises.

In this article, we argue that the current Chinese pension arrangement represents a case of incomplete universalism. Although the Chinese central government has created a pension arrangement featuring universal coverage, we find: 1) its benefit level is low; 2) the benefit level varies from region to region; and 3) the phenomenon of the "policy-bundle" (*zheng ce kun bang*) is widespread among pension program in rural China. These factors make the so-called universal coverage weak and incomplete.

2 The pension arrangement in modern Chinese history

2.1 Old age security in urban areas: from labour insurance to social insurance

In China, the first old-age pension program was introduced soon after the founding of the People's Republic of China (PR China), when the Communist government began to reform the country in the image of its own Marxist-Leninist ideology. The central reform policies in the post-revolutionary period concerned land reform, the collectivization of agriculture, and the establishment of a labour insurance system. In 1951, the State Council of PR China adopted the 'Labour Insurance Regulation' (Dixon, 1981), which stipulated the creation of a comprehensive labour insurance system protecting industrial workers in state-owned enterprises (SOEs) against the social risks of illness, work accidents, disability, maternity, and old age. The labour insurance contributions were paid solely by the SOE, and all enterprises were legally obligated to transfer 30 percent of the contributions to the All-China Federation of Trade Unions (ACFTU). The ACFTU assumed the responsibility to pool and redistribute the labour insurance funds at the national level. In this period, industrial workers and civil servants in urban regions were covered by an old-age protection program through their employment in SOEs and state administration. Customarily, each SOE was responsible for paying out old-age pension benefits to employees who had reached the statutory retirement age of, at the time, 60 years for men, 55 for female civil servants, and 50 for female workers (Dixon, 1981; Mok, 1983).

The adoption of the reform and opening-up policy in 1978 was both a social and economic turning point for modern China. The successor of Mao, Deng Xiaoping and his reform-minded colleagues, declared the end of the Maoist leftist course and steered the Chinese economy towards a more liberal, market-oriented system. This recalibration of the economic course eliminated the centrally planned economy and had a significant impact on social protection in China. State-owned enterprises became responsible for their own profits and losses, and they were increasingly considered independent legal entities. The social pooling through the ACFTU had collapsed with the market liberalizations, since now each enterprise, regardless of whether it was an SOE, a private enterprise, or a joint venture, was responsible for paying its employees' pensions out of its own funds. As a result, SOEs whose proportion of elderly employees was large found themselves in serious financial difficulty, usually resulting in delayed pension payments. The pension burden in the wave of the privatization of SOEs had thus become one of the most serious social challenges since the adoption of a socialist market economy (Feldstein, 1999). In fact, many bankrupted enterprises in China's heavily industrialised regions were unable to provide pensions for retirees. In the 1980s-90s, these delayed and suspended pension payments led to many demonstrations and protests by retirees in urban regions, jeopardizing social cohesion and undermining the legitimacy of the Communist rule (Chen and Rösner, 2000). Conventionally, the old-age grant for retirees had been considered a reflection of the superiority of the Communist welfare system and with that, the ruling party guaranteed the loyalty of the working class to the Communist government. The pension arrangement and its reform in urban China became a highly politicised and ideological issue among the public because it so closely related to political stability and the socialist legacy in China.

Since 1991, following a series of local pilot projects at the sub-national level, the State Council of PR China endeavoured to spread a two-pillar pension arrangement for urban employees across the country, which was in line with the mainstream trend of global pension reforms pushed by the World Bank since 1994.[1] The statutory pension arrangement labelled as a partial funding system in the Chinese context was based overwhelmingly on two pillars. The first was an earnings-based pension based on the pay-as-you-go (PAYGO) principle, with a defined benefit portion, and the second was a defined contribution portion, which relied on mandatory individual savings (Feldstein 1999). Both pillars were income-centred and financed by the contributions of employers and employees. The employers paid 20 percent, and employees 8 percent, of gross monthly earnings as old-age pension contributions (Fan 1999).[2] In the initial stage of the creation of this modern old-age insurance program, only a small number of employees were covered by the new scheme. However, by 2005, roughly 55.2 percent of urban employed workers, accounting for 30 percent of urban residents, were covered by this program (Liu, 2005). Since its inception, step-by-step, the old-age insurance program incorporated more blue-collar and white-collar workers into this scheme.

The partial funding plan was considered an innovative way of instituting a suitable pension model in China. The mainstream opinions of the scientific community advocated the advantages of a partial funding plan (Fan 1999; Chen and Rösner 2000; Liu 2005). On the one hand, the PAYGO arrangement can achieve the target of intergenerational transfer via social pooling; on the other hand, the goal of funding contributes to the improvement of personal responsibility and capital accumulation in individual pension accounts. Compared to a single-pillar pension scheme, the two pillars of the pension arrangement are flexible and sufficient to overcome the rigidity of either the PAYGO arrangement or the full funding plan. The former is highly associated with the dependency ratio and thus is easily prone to population ageing. Simultaneously, the latter is determined by the private accumulation of funds, which easily results in inequality among retirees' pensions. Another disadvantage of a full funding plan is its exposure to fluctuation in the financial market. Various scholars believe that the partial funding plan is a suitable model that combines the advantages of the PAYGO arrangement and the full funding plan and eliminates their disadvantages (Chen and Rösner 2000).

One of the biggest challenges in adopting an additionally funded pension is the guarantee of the current needs of pensioners who had never contributed to an individual pension account. Diversion of pension funds from individual pension accounts by various local governments has been a policy option to finance the needs of current retirees, causing the so-called problem of 'empty accounts'. In other words, the accumulation of pension funds exists on paper in the accounts; however, in reality, the accounts are usually empty because the funds have been diverted for the purpose of financing the current demands of retirees.

2.2 Old age security in rural areas: pilot projects and their failure

Compared with the urban old-age insurance system, the rural pension program was a 'latecomer'. Originally, traditional thinking did not endorse the creation of a rural old-age insurance program. The conventional wisdom that old-age security was an individual and family matter and the idea that one should raise children in preparation for one's old age was widespread in rural China. These Confucian values supported old-age protection through members of the extended family. However, these traditional notions became anachronistic since the grand social and economic transformation in China, which saw a decline in birth rates, immense migration from rural to urban areas, and a decline in family size. By the end of the 1990s, old-age protection in rural China became a matter of concern for the Chinese government as well as for international and supranational organizations such as the Asian Development Bank (ADB). The State Council and the ADB initiated several pilot projects in 1999, aimed at the creation of an old-age insurance program in rural China. Liu (2000) has elaborated the necessity of creating a rural old-age pension program from a functionalist perspective, and Leisering, Gong and Hussain (2002) have discussed the feasibility of a rural old-age pension program and pleaded for filling the social security gap among the rural elderly.

Unlike the urban old-age insurance program, the rural program was based on one sole pillar: a funded, defined-contribution pension plan (Shi, 2006; Liu, 2005). The rural old-age pension program designed via various pilot projects had a voluntary rather than a mandatory flavour. Rural residents could choose to pay a contribution of between 2 and 20 yuan (0.33 and 3.3 US dollars) monthly, quarterly or annually, and the benefit level of the pension was dependent on the accumulating pension funds and investment returns. Rural residents would enjoy a pension at their retirement age, receiving payments monthly or quarterly. However, they were not legally obliged to participate in the experimental rural old-age insurance program. Compared with the urban social insurance program comprising a mandatory PAYGO portion and a mandatory funding scheme, the rural old-age insurance lacked a social pool. The benefit level was decided entirely by personal payments into individual accounts. Thus, the pension entitlement of rural residents was unevenly distributed among regions, with people of different ages and social classes having different capacities to pay (Shi, Miao, and Wang, 2001; Liu 2005).

Due to a lack of trust among rural residents in private pension plans, this rural pension arrangement failed to take root. The number of participants peaked at 80 million in 1999, which accounted for only 11 percent of the rural population, and thereafter, steadily decreased as rural residents withdrew their payments from their individual accounts. By 2004, this number had dropped by one third, with 53.89 million rural residents participating in the rural old-age insurance scheme, resulting in the failure of this experiment (Liu, 2005).

3. Recent developments in the pension arrangement

3.1 A national pension plan in a new pension republic

Despite considerable efforts since 1991 to develop and expand the urban old-age insurance program, the domain of old-age security has been plagued by problems. First, nearly the entire rural population, which amounts to 800 million citizens, was excluded from the urban old-age insurance program while, as mentioned above, only a small number of rural residents were covered by the rural old-age insurance scheme through local pilot projects. Further, considering that the urban pension program was earnings-related, those who were not steadily employed but worked only part-time or intermittently were inexorably excluded from the urban old-age pension program. Consequently, the pension arrangement in China had a huge coverage gap until 2005.

In 2002, a generational change took place inside the Communist Party of China (CPC), as new reformist leaders Hu Jintao and Wen Jiabao came to power. The Hu-Wen administration fundamentally adjusted the neoliberal course of their predecessors by means of immense investments in the domain of social protection. This new policy was dubbed the 'care-for-the-people policy' by Chinese media, and it highlighted the role of social policy, social protection, social welfare, and the improvement in the well-being of socially vulnerable groups like migrant workers (Sun & Liu, 2014). The successor of the Hu-Wen government, the Xi-Li government (Xi Jinping and Li Keqiang), has even further promoted the equalization of public services to narrow the social welfare gap, not only among regions but also among social classes. This novel policy contributed to the expansion of social expenditures, extension of the social welfare system, and empowerment of the weak and vulnerable. Along with this expansion of the Chinese welfare sector, the pension arrangement had also been restructured and reorganised, expanding the degree of coverage significantly.

The new normative value of pension reform drew upon the ideas of equity and equality. Reformist elites under the Hu-Wen administration adhered to the value of universalism when seeking to create a novel basic and non-contributory pension for all those who had not yet been covered by the social insurance program. The new grand transformation stemmed from a 2008 pilot project in the city of Baoji, in the northwestern province of Shaanxi, where the local administration experimented with a new pension scheme by covering local rural residents via a social pension funded through the tax revenues of the local administration. Besides the basic pension, rural residents were encouraged to participate in a funded pension plan, which was heavily subsidised by local governments. As a result, rural residents of Baoji have been covered by a two-pillar pension plan. This new pilot project was referred to as the 'Baoji-Model', and it has been emulated by dozens of cities (Qing, 2009).

In 2009, the Hu-Wen administration decided to set up a pension plan in rural regions, called the 'New Rural Social Pension System', which combines a highly subsided personal savings plan and a non-contributory basic pension for the rural population. In 2011, the Chinese State Council set forth an ambitious national plan to create a basic pension for non-employed residents in urban regions, combining a funded pension financed by individual payments and subsidies from the governments. In 2014, under the Xi-Li administration, the State Council decided to merge the Urban Residents Pension Plan and the New Rural Social Pension System into a unified basic pension insurance plan for urban and rural residents; most rural residents and non-employed urban residents were now covered by one national social pension plan.

The new universal pension plan is distinctly different from previous pension arrangements. First, this new pension is a non-contributory pension, disconnected from personal payments, pension contributions, and working career. Recent studies regarding this kind of social pension scheme indicate that this program is one of the most popular programs of social cash transfer among developing and transition nations (Leisering 2009). However, most of these nations have adopted a means-tested social pension, in which only impoverished older people in need are entitled to a social pension (such as in the case of India, South Africa, and urban areas in Brazil; see Leisering, Buhr, & Traiser-Diop, 2006). Only a small number of nations, including China, have adopted a universal non-means-tested pension. The third feature is a comparatively low benefit level. The social pension in China amounts to barely 9 US Dollars monthly (the local government can top up this minimum benefit), while the benefit level of the social pension in South Africa and Brazil is comparatively high (128 US Dollars and 318 US Dollars per month respectively) (Weible, & Leisering, 2012; Barrientos, 2013).

3.2 Analytical overview of recent pension reforms in China

Through the creation of the universal pension scheme, theoretically, each Chinese citizen is entitled to participate in the pension arrangement as of 2014. Despite the scope of universal coverage, the depth of universalism is insufficient or ‘incomplete’. Meanwhile, with the introduction of new pension reform in 2015 and the previous fusion of the rural and urban social pension schemes, it is encouraging to see the stratification of the Chinese pension arrangement is becoming flattened. A trend analysis of recent pension reforms is presented as follows.

The ‘Ordinance establishing a unified basic pension insurance system for urban and rural residents’ was adopted in 2014. This reform attempts to merge the two pension schemes in urban and rural China into a universal one. This pension plan is based on a non-contributory social pension and a personal pension heavily subsidised by governments at different administrative levels. Nearly 498 million people were covered by this pension plan by the end of 2013 (MOHRSS, 2014b). With the introduction of this pension plan, the Chinese government has realised the political will of a universal coverage pension arrangement. However, we argue that the so-called universal coverage represents a case of ‘incomplete’ universalism for three reasons.

First, the benefit amount of this plan is very low, with a country average of 81 yuan (13 US dollars) per month (MOHRSS, 2014c), which is much lower than the benefit level of other forms of social assistance such as the Minimum Living Standard Schemes.

Moreover, the pension plan reflects enormous regional disparities. The central government has set the benefit level at a minimum of 55 yuan (9 US dollars) per month, but local administrations can add supplementary remuneration according to their financial condition or the local cost of living. Thus, the benefit levels vary between regions. Figure 1 illustrates the pension benefits of several cities, with Shanghai setting its pensions at 540 yuan (88 US dollars) per month, whereas in Kunming, pensioners receive 84 yuan (14 US dollars).

Finally, the pension plan in rural China can be deemed conditional due to the phenomenon of the ‘policy-bundle’ (*zheng ce kun bang*). Some studies have noted that this distinctively Chinese phenomenon is prevalent in certain rural regions: in a household, the elderly can only receive a monthly social pension if their adult children have already participated in the rural old-age insurance program (Yang 2010; Mei 2010). Local party cadres have used the new social pension scheme as a coercive method, obliging middle-aged rural residents to contribute to local pension arrangements. This local practice has been widespread in those regions at the lowest level of the administrative structure (counties, townships, villages), where the participation rate for contribution-based rural old-age insurance programs is comparatively low. The social meaning of 'universalism' has thus been partially weakened. Through this deliberate bundling of pensions, the participation rate may increase, which is considered a political achievement for local party cadres. The emergence of the policy-bundle confirms a famous Chinese idiom: higher authorities have policies; localities have countermeasures (*shangyou zhengce, xiayou duice*). However, this policy-bundle remains a local practice, which has been widely criticized in social media for its lack of legal foundation (Yang 2010). Some provinces, for example Shandong province, have taken measures to abandon this practice, enabling local residents to file a complaint at the provincial office of Human Resources and Social Security if the local governments oblige adult children's participation in order to let their parents receive the pension.

The latest pension reform in China was instituted on January 14, 2015. The State Council issued the 'Decision concerning pension reform in the government and public institutions', which represents a historical milestone for China's pension arrangement. It provides for abolition of the wholly state-funded government pension and the end of the dual urban old-age pension arrangements. Around 40 million civil servants and public sector employees (such as teachers, doctors, and science researchers),[3] have been brought under the same pension rules as employees in enterprises,[4] and they must make pension contributions. That is, employees must pay 8 percent of their gross income, while administrative and public institutions pay another 20 percent as pension contributions.

This reform strips civil servants and public sector employees of their privileged status, and the inequality between them and employees in enterprises is eliminated. Chinese Vice Premier Ma Kai stated, ‘This reform will make the social pension scheme fairer and more sustainable’ (GOV 2015). It is worth noting, however, that pension stratification among different social classes still exists, for example, in the difference between urban residents, rural residents, and migrant workers.

4. Conclusion

This article has analysed the pension arrangement in China, discussing its recently established universal, non-contributory pension scheme. We have characterised the recent pension reform as a case of flattened stratification and incomplete universalism.

The Communist pension program in the Mao era was a stratified system associated with the social welfare classes in the Communist hierarchy and based on Communist welfare ideology. Since the reform and opening up, the pension arrangement in China has retained its stratified and unequal nature, and the past pension legacy has shaped subsequent reforms. Recently, the Chinese government has made significant efforts to institute pension reform, which has led to the remarkable achievement of universal coverage, by entitling formerly excluded rural residents and non-employed urban residents to a universal, non-contributory pension (see Table 1). Nearly 860 million Chinese residents have been covered by one of the three pension schemes, which accounts for 86 percent of the total adult population. The urban pension programs have already achieved nearly full coverage of the urban adult population. Currently, some 463 million rural residents, or an estimated 80 percent of the total rural adult population, are covered by the new social pension scheme, which had covered only 33.26 million rural residents in 2009. Despite the ostensible universal coverage, we argue that the recent reforms reflect flattened stratification and incomplete universalism.

First, although the Chinese pension arrangement remains stratified, it is less stratified than before (Figure 2). Through the elimination of the dual urban pension program and the establishment of a unified non-contributory pension in both urban and rural regions, the stratification of the Chinese pension arrangement has been flattened. For instance, the wholly state-funded government pension for civil servants and public sector employees has been abolished, making them subject to the same pension rules as employees in enterprises.

Second, despite the government's assertion that a pension arrangement with universal coverage has been established in China, we argue that it is actually a case of incomplete universalism. Even though the scheme purports universal coverage, the depth of the universalism is insufficient. First, the benefit level of social pension is very low, 81 yuan (13 US dollars) per month on average. This amount is far less than enough to ensure a basic livelihood for elderly people, and in many cases, it is much lower than the benefit level of other forms of social assistance. Moreover, the benefit level varies from region to region. For example, the pension benefit in Shanghai is five times higher than that in Kunming. Finally, the 'policy-bundle' found in some parts of rural China mitigates universal coverage by tying the receipt of a pension to the coercive participation of beneficiaries' adult children in the rural old-age insurance program. This bundling of policy has thus made a so-called universal pension a conditional one in some regions.

Historical experiences from Western welfare states and global pension reform suggest that a universal pension arrangement does not necessarily mean more redistribution and better old age protection; for example, an extremely low level of universalism can also result in the shifting of state responsibility to the private savings of individual households. The state has merely defined the minimal responsibility for the protection of its citizens, leaving the major task of old-age protection to the individual. In this vein, a low level of universalism can also justify a minimal degree of state responsibility or even state retrenchment. It is still uncertain how China will develop in the future; much depends on how the notion of "universalism" will continue to be defined by the Chinese epistemic community. Clearly, more researches are needed to explore prospective pension development.

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[1] In ‘Averting the old age crisis: Policies to protect the old and promote growth’, the World Bank pleaded for a multi-pillar pension system involving a tax-financed basic pension as the first pillar, a mandatory funded pension as the second pillar, and private savings for retirement as the third pillar (World Bank, 1994).

[2] The contribution rate has constantly changed after the adoption of the partial funding system; currently, employers pay 11 to 20 percent of the employees’ gross income, and employees contribute 8 to 11 percent. The contribution rates vary slightly according to region (Wu, 2013).

[3] Veterans who have left the army must make pension contributions in their new workplace, just like other employees. The only bonus for their military service is that the period of service is considered a pension contribution period.

[4] See the ‘Circular extending the reform of the old-age insurance system to employees of the private sector’. In 2013, 322 million employees in enterprises participated in this pension plan (MOHRSS, 2014a).

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