



People's Republic of China
Old-Age Pensions for the Rural Areas:
From Land Reform to Globalization

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Lutz Leisering
Gong Sen
Athar Hussain

Asian Development Bank sponsored a Small-Scale Technical Assistance No. 3607 to launch work on PRC: Policy Support for Social Security Reform under the Tenth Five-year Plan. This TA has been managed and supervised by Ms. Shamshad Akhtar, Director, Governance, Finance and Trade Division, and Mr. Ying Qian, Principal Financial Economist. The contributors to the report include: (i) Lutz Leisering, a professor at University of Bielefeld, Department of Sociology, Germany; (ii) Gong Sen, a Ph.D. Candidate at the University of Sheffield, United Kingdom on study leave from the Ministry of Labor and Social Security, PRC; and (iii) Athar Hussain, a research fellow at the Asia Research Center, London School of Economics and Political Science, United Kingdom. The work profited greatly from the generous support given by Directors Wang Xuepeng, Li Dajian, Yuan Jiaomin and Jiang Bingyi of Yantai Municipality, Shandong Province, Director Wang Xiaobo of Yunnan Province, and Director Zhao Dianguo of Ministry of Labor and Social Security, Beijing. Technical support in Beijing was provided by Professors Chen Youqi, Hai Chunxing, and Wang Zongfan of Forestry University, Professor Song Xiaowu of State Council Office for Economic System Restructuring, Professor Peng Xizhe of Fudan University, Mr. He Ping of Ministry of Labor and Social Security, Professor William Hsiao of Harvard University, and Ms. Catharine Martin of Department for International Development, UK.

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FOREWORD

The Asian Development Bank (ADB) has financed several technical assistance projects to help the People's Republic of China (PRC) in reforming its social security system and strengthening institutional capabilities. The State Development Planning Commission, the country's primary economic planning agency, requested ADB's assistance to develop a comprehensive social security reform program to support the preparation of the Tenth Five-Year Plan (2001-2005). The Plan called for the development of a multi-pillared social security system covering both urban and rural areas.

The technical assistance study examined options and strategies for introducing unified pension and medical insurance schemes in rural areas. The studies were conducted during March - July 2001. Overall strategic direction and supervision of the study was provided by Ms. Shamshad Akhtar, Director, Governance, Finance and Trade Division of ADB and Mr. Ying Qian, Principal Financial Economist of the same division. Two reports for rural pension and rural medical insurance were prepared. A workshop was organized jointly by ADB and the State Development and Planning Commission on 9 - 10 July 2001 in Beijing to discuss draft final reports.

The process of economic restructuring has affected both the level of rural incomes and rural and urban income differences. The rural pension report provides an analysis of issues ranging from economic, demographic and urbanization to experiences of pilot rural schemes and rural pension administration both at central and local government levels.

The report highlights that one of the major issues impeding the development of rural pensions is the absence of a supportive policy and institutional framework. The traditional arrangements for old age protection, mainly in the form of family support and land, are increasingly becoming less dependable. At the same time, new arrangements such as basic pension schemes and commercial insurance are not yet developed in rural areas. The report argues that because of increased labor mobility and erosion of the distinction between rural and urban populations, there is a need for a national pension scheme covering both urban and rural areas. A phased approach is recommended to improve participation, build up efficient and accountable administration, and increase support by the central Government.

In the course of the study, the authors, Messrs. Lutz Leisering, Gong Sen and Athar Hussain, visited several rural provinces to evaluate local pilot pension programs, and held discussions with local government agencies and other stakeholders. The authors also had extensive discussions with central Government agencies and research institutes including the Ministry of Finance, Ministry of Labor and Social Security, and the Chinese Academy of Social Sciences.

This report is being published at the request of the PRC Government to disseminate the findings of the study to a wider audience – government officials, academics, bilateral and multilateral development agencies. Special thanks are due to the various contributors, Ms. Hou Yan of the State Development and Planning Commission for her commitment and relentless support of the project. The authors are indebted to the administrators and scholars interviewed as part of the research. Lastly, Ms. Edna Gonzales coordinated the publication of this book and Mesdames Corazon Murakami and Jessica Ebio provided administrative support.



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Plan of the Report

The report proceeds as follows: **Chapter 1** reviews the need for setting up an old-age pension scheme in rural People's Republic of China. This step is necessary because, unlike health services, some people question if the PRC needs rural pensions at all.

Chapter 2 summarizes the state of affairs, i.e., the current system of old-age pensions in the PRC, and delineates the development since the early fifties.

Chapter 3 provides a conceptual framework for models and rationales of old-age security in rural areas.

Chapter 4 looks at the experiences of other countries in the field of rural pensions.

Chapter 5 describes the counties visited and the research design of the project. We conducted field visits in three types of counties: well-off counties in Shandong Province, a poor county in Yunnan Province, and an average county in Hubei.

Chapter 6 highlights the key issues of the current reform debate, first with regard to the current system of provision, which is based on family support, land, and pilot pension schemes in selected areas; and second with regard to the problems of inequality and the environment of pension policies. The chapter includes broad evidence from the field visits.

Chapter 7 sets out policy options and strategies, translated into a practical plan for action in **Chapter 8**.

Unlike urban pensions, rural pensions are nonexistent (except the pilot schemes) in the PRC and the question is whether to set up a system because there is no consensus if a rural system should be set up at all. While providing the relevant quantitative figures and calculations, this report put emphasis on conceptual, qualitative, and policy-oriented questions. The problems of rural pensions are not only a matter of demographic ratios and financial management.

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Abbreviations

ACFTU	All-China Federation of Trade Unions
CAB	Civil Affairs Bureau
CCP	Chinese Communist Party
COE	collectively owned enterprise
FYP	five-year plan
LSSB	Labour and Social Security Bureau
MLSS	Minimum Living Standard System
MOCA	Ministry of Civil Affairs
MOL	Ministry of Labour
MOLSS	Ministry of Labour and Social Security
NBS	National Bureau of Statistics
NGO	nongovernment organization
PAYG	pay-as-you-go
PRC	People's Republic of China
SC	State Council
SDPC	State Development Planning Commission
SFPC	State Family Planning Commission
SOE	state-owned enterprise
TVE	township and village enterprise
Y	yuan

EXECUTIVE SUMMARY

1. Why Rural Pensions? Need for Political Action

The society of People's Republic of China (PRC) rests on a notion of divided citizenship. Rural and urban are sharply distinguished. The distinction is politically and legally created and reinforced by a strict separation between two kinds of social organization and by various checks to migration from the countryside to the cities.

The organization of social security not only reflects this divide: It is part and parcel of it. Social policy is a major device in constructing and deepening the rural-urban divide. Schooling, housing, and public infrastructure is organized on a different basis, and there are fundamentally different institutional arrangements in health services and old-age security. Whereas urban citizens enjoy a generous system of old-age pensions introduced early in the 1950s and surpassing the usual standards of developing countries, there are no public provisions for old age in rural areas except marginal social assistance.

Talking about rural pensions is not talking about reform but about setting up a system where there has been none before, except pilot schemes. In the public debate there is no consensus whether a rural system should be established. Family support and land are invoked as traditional forms of support in old age that should continue to play this role in the future. Moreover, for rural pensions there seems to be no immediate economic pressure comparable to the reform of state-owned enterprises in urban areas that triggered the urban pension reform.

Nevertheless, there are four major reasons for considering to set up old-age pension schemes in rural areas in the PRC:

- the decline of the number of children and the foreseeable ageing of the population
- socioeconomic change in the countryside: over the last 20 years, a silent revolution has taken place—Almost one third of the rural workforce is not "rural" but is mainly employed as wage laborer in the local industry; the rural-urban distinction is further blurred by the marked increase in migration to towns and cities;
- the long-term character of pension policy; and
- the need for a central political decision after years of uncertainty about the existing pilot schemes.

Pensions have a wider significance beyond contributing to a living for the elderly: they can be a step towards nationbuilding, especially in a still young nation like the PRC. Social security can help unite the country and bridge the division between the "two nations"—urban and rural. Historically, path-breaking welfare reforms have often been linked to crucial stages in the process of nationbuilding. The foundation of modern social insurance by Bismarck in the 1880s was a major component of consolidating the then new German nation. The foundation of the British "welfare state" in 1945–1948 emerged out of a feeling of national unity during and in the immediate aftermath of the Second World War.

2. Public Pension Policy in the PRC since 1949—A Changing Social Contract

The pension system and pension policy in the PRC falls into three almost entirely unrelated parts:

- a system for urban enterprise workers;
- a system for the rural population; and
- a system for public sector personnel such as cadres, civil servants, and servicemen.

The three components have totally different institutions, benefits, and finance; are operated by different departments and sections of government; and were established at different points in time. Therefore there are three histories of public pensions in the PRC that have rarely touched each other. This tripartite division expresses a basic social contract of the PRC society about the rights and duties of different groups in society.

The contract emerged in the historical situation of liberation in the late 1940s and early 1950s. On the eve of the new PRC when a provisional constitution was being drafted, Chairman Mao Zedong argued that, since the farmers had got the land after the liberation, the urban workers should also benefit from the victory of the revolution and receive comprehensive social security. This social contract laid the foundation of the PRC social security system. Public social security for urban workers was part of nationbuilding while for the rural population land and family acted as old-age security.

The Seventh Five-Year Plan (FYP) proposed to establish an embryonic form of social security system in the PRC in 1986–1990. This was the first time the term social security was adopted at such a top level.

Since the 1980s, the need for state-owned enterprise (SOE) in the urban sector reform has been a major driving force of pension reform.

The year 1991 saw the breakthrough in rural old-age security—the introduction by the Ministry of Civil Affairs of pilot pension schemes in rural areas. They operated in a modest way like organized saving but introduced the idea of formally providing for old age to the countryside.

By the end of 1997, 2,008 counties and 285 prefectures (except Tibet) had begun the undertaking. Moreover, more than 57% of townships or towns, almost all counties, a little less than 75% of prefectures, and 87.1% of provinces had established special administrative organizations at the related levels. There was an administrative system from the bottom to the top by the end of 1997.

In the late 1990s the system was adversely affected by external influences. In the wake of the Asian financial crisis and the rectification in the insurance industry, some leaders said that it was too early and too risky to introduce public pensions in the rural PRC. Local administrators and participants soon became demotivated by the lack of support of the central government. However, at the same time, the reform of the urban system was actively promoted.

By 2001 three new ideas figured in the debate: A compromise proposal by the Ministry of Labour and Social Security to combine the pilot schemes with commercial fund management, the inclusion of township and village enterprise (TVE) workers in the urban system, and a State

Family Planning Commission scheme that provides pensions for one-child and two-daughter families.

The socioeconomic changes of the reform area since 1978 have been eroding the ingrained Chinese social contract but no new contract has emerged as yet. The period of political non-decision lingers on.

3. Providing for Old Age—Why and How?

Beyond providing for the elderly, pensions are useful for individuals and for the economy in several ways:

- they provide security over the individual life span (for the young and middle aged);
- they relieve obligations toward the elderly (for the middle aged);
- they create personal autonomy in old age (for the elderly);
- they are an instrument for regulating the labor market because they create an age of retirement that divides working life from retirement; and
- they discipline people in their consumption behavior by forcing them to use part of their current income for future purposes.

This means that pensions are not only about doing good and a cost factor but they have also economic utility.

There is a range of objectives and values that can guide pension policy, some of them conflicting. The four main objectives of pension policy are

- poverty reduction and equality;
- security (that may entail the reproduction of inequalities);
- high coverage (that is a problem particularly in developed countries); and, more recently,
- high returns.

There are three main normative criteria on which pension entitlements can be based: achievement, merit, and need. Unlike most other developing countries, the PRC has a pronounced tripartite structure of its public welfare provision system that encompasses all three normative orientations:

- merit-based schemes for public sector employees like cadres, civil servants, and servicemen (excluding SOE employees), with fairly generous benefits to secure their active support of government;
- achievement-based schemes, mainly an unusually generous urban old-age pension scheme that caters for the industrial class base of socialism;
- need-based schemes that provide for those who have no other private or public income, such as Five Guarantees and poor relief at the village level and more recently the Minimum Living Standard System (MLSS).

The system becomes more complex by the division rural-urban in welfare provision that cuts across the tripartite structure.

In setting up rural pensions, it is therefore important to have the whole structure of the welfare state in view (integrated policy), to be open to revising institutional structures that have grown become ineffective over the past decades. The current reform of the urban pension system and the MLSS are first steps, but the rural system and the merit-based systems for public sector officials ought to be included in an overall reform plan, too. Different departments

of government that are responsible for different components of the structure should increase cooperation and coordination. This is currently little developed.

4. Learning from Other Countries

Since the PRC's endeavor to set up formal rural pensions is unique among developing countries, little can be learned from other developing or transitional countries. From the history of European rural pensions, however, much can be learned with regard to urgent questions

- Is it too early to introduce pensions in rural areas? Did Western countries not adopt provisions for farmers at a later historical stage?
- Is it too risky? What long-term risks do we run when establishing a formal commitment to providing for the rural elderly? Are we facing soaring expenditure, especially in this subsidy-prone clientele? Are we eroding the traditional work discipline of farmers? Are we unleashing a growth in bureaucracies, clientele, and benefits?
- Which institutional design would suit the needs and conditions of this specific group? Should farmers be covered by a separate system or rather join other systems? How should pensions be financed considering that farmers are not employed and what benefits are conceivable in the face of low resources among this group?

The first and most basic message from European experience is—No, it is not too early to set up rural pensions because several European countries started equally early or even at a far lower level of economic development. Further, such undertaking is risky, but all European countries took the risk because the process of modernization produced a need for pensions in every country. From this experience it is not likely that the PRC will be able to avoid that risk much longer. The Danes came first (1891). Together with Germany, which introduced old-age insurance (for industrial workers) in the same year, the Danish system was the first (general, not only rural) old-age security systems in any country. Modern social policy began with farmers! It was not, as normally assumed, the workers movement and social democracy but the landed classes who first pressed for welfare provisions in Scandinavia.

Although there is no agrarian bourgeoisie in the PRC, the message is—it is not the level of economic development that matters but politics. If the political leaders decide to install pensions for farmers they can do it, even at a very low economic level. But unlike the landed classes in Scandinavia, the PRC farmers have no voice in politics, no lobby.

The urban workers, by contrast, have always had a strong lobby. It was in the interest of government to privilege them. Therefore, the urban workers have enjoyed a pension scheme that was and still is much "too early," judged by the level of the PRC's industrial achievement.

Another key lesson is that massive government subsidies to farmers' pensions could not be avoided in any European country. These subsidies can make up as much as 70% of total spending of the Ministry of Agriculture (in Germany). The reason is the decreasing number and the ageing of the rural population and their relative poverty.

A third lesson concerns the relationship between social policy on the one hand and economic and agricultural policy on the other. Governments pursue social security not only for moral but also for economic reasons. Pensions are an instrument for the development of the rural economy.

Pensions for farmers can promote the modernization of agriculture toward increased productivity and downsizing by tying pensions to a change in the management of the farm: farmers can receive a pension only if they give up farming. Through compulsory retirement, pensions have also been an instrument of reducing labor supply and helping cut the rural surplus labor.

5. From East to West, from Rich to Poor—the Counties Visited

The team leader and the domestic expert visited four counties: Zhaoyuan City, Muping District (Shandong Province), Wuding County (Yunnan Province), and Huangpi District (Hubei Province). The four counties represent a mix of rich, middle, and poor areas. Wuding is one of the 63 nationally defined poverty counties in the province, or one of the 594 poverty counties in the whole country. Chapter 5 describes the economic, demographic, geographic, and social contexts of pension development.

6. Key Issues of Reform

This Chapter highlights the key issues of the current reform debate: first with regard to the current system of provision, which is based on family support, land, and pilot pension schemes in selected areas; and second with regard to the problems of inequality and the environment of pension policies. The Chapter includes broad evidence from field visits.

a. Can Family and Land Still Provide for Old Age?

The traditional security system in the PRC countryside is based on the family and an owned land plot. Socioeconomic changes seen in recent years have weakened the traditional system and created the need for a new one.

There is little doubt that the allocation of land to rural households has been an important source of economic security to the rural population. Without the allocation of land to rural households, poverty in rural areas would have been much higher than it is now. Looking into the future, the level of economic security provided by land will continue to diminish. With cultivated land area fixed, the gap between income from farming and income from industry and services has widened. The only way of arresting and eventually narrowing the gap is by consolidating land and increasing the size of landholdings. There is a conflict between maintaining the social welfare role of land—which requires dispersed distribution of land—and raising farm income—which requires a concentrated distribution of land. The conflict will become more pronounced and its resolution requires a gradual phasing out of the social welfare role of agricultural land.

b. The Ministry of Civil Affairs/Ministry of Labour and Social Security Pension Schemes for Farmers: Success or Failure?

In the late 1990s criticism of the rural pilot pension schemes by influential people at the center became more serious, especially in the wake of rectifying the insurance industry. Forced participation of farmers, misuse of pension funds, and bad management were the main charges brought against the schemes. This section aims to evaluate the pilot schemes in the light of the criticism raised and beyond.

A 1995 evaluation group gave a positive evaluation of the schemes. It argued that it is necessary to develop a formal arrangement in the rural sector to supplement the family support and individual efforts in old age, and that the Ministry of Civil Affairs (MOCA) plan would be workable in those localities with developed economy and solid administrative bases at the grass roots. Moreover, it seemed to the group that the schemes had made some positive contributions to population control, social stability, and economic development in the pilot areas.

On our field visits, we found that there is little solid evidence that could support the far-reaching criticism brought against the scheme. The day-to-day administration in rich areas like Yantai seems reliable, computer-aided administration is routine at the county level, and pension fund investment is also efficient.

Problems of the schemes include participation, which has been low in poor areas. In regards to outcomes, it is apparent that contributions and benefits are low in poor areas like Wuding but also for many participants in better-off areas. Contributions are sometimes made only once a in lifetime. These are embryonic "pensions." The scheme has neither defined benefits nor defined contributions. It is a form of organized saving rather than social insurance.

Achievements, however, dominate.

Objectives and outcomes: The original policy concept by MOCA is realistic with regard to the aim of enhancing old-age security in the countryside by pensions as part of a broader income mix. Even at the current low level, the benefits received by the pensioners make a difference for many of them.

Institution building: The schemes are not social insurance but rather an organized saving plan for farmers. Compared with other developing countries, this is an achievement.

Administration: A standard operational procedure has been established, particularly but not only in well-off areas.

Acceptance: The pension schemes have been widely promoted and have been accepted by many farmers.

A key conclusion is that the performance of individual pension schemes depends heavily on local economic conditions. Finally, many problems accompanying the rural pension development are politically induced, such as insufficient encouragement to participants and administrative staff, little coordination between government departments, and, above all, the current destabilization of the system by a protracted period of nondecision.

All in all, this is a workable scheme, though with a limited design—a kind of organized saving—that may just for this limitation be suited for an economically developing area.

c. The Modernization of Rural PRC—Toward Undivided Citizenship?

Over the last two decades new social institutions have emerged in PRC's rural society: the household responsibility system, TVE, and grassroot democracy in the villages based on villagers committees and villagers meetings. The most recent institutional innovation is the introduction of public provision for old age, namely the piloting of pensions by MOCA since 1991, and, notably, the adoption of the older urban pension scheme in some rural enterprises. The operation of public pensions is closely linked to TVEs.

Since the 1980s TVEs have been a major factor of the growth of the rural economy and the PRC economy at large. It has been much unnoticed that in the 1990s TVEs have also become a major factor of old-age security in the rural PRC.

On one hand, the proliferation of TVEs is challenging the pilot schemes for rural pensions: the underlying assumption that the pilot schemes address farmers has become invalid. Many people have become employees of factories and enterprises with marginal concern for the piece of land they still may have got.

On the other hand, the TVEs play an active role in the operation of the pension schemes although this role has never formally been assigned to them, such as paying subsidies, organizing the collective entry of workers, or cooperating with the local labor bureaus. Moreover, villages often pay subsidies out of the profits of their TVE. The village organization is another pillar of the pension schemes.

TVE and migration blur the distinction rural - urban. At present there is a confusion of who shall be included in which pension scheme (urban or rural). Household registration (*hukou*) is less and less suited as a basis of organizing old-age security.

Pension entitlements are not only a benefit to the entitled, they may also benefit the TVEs in economic terms. Pensions have three functions for a TVE: attracting qualified personnel by offering subsidies; controlling the workforce through selective subsidies; and the use of pensions by TVE managers as another way of enriching themselves, by arranging for high company subsidies to their own pension account.

The triangle pensions—village organization—TVE entails new patterns of inequality and social exclusion in several dimensions:

- villages with TVEs versus those without or with weak TVEs;
- poor areas with few TVEs versus richer areas with many;
- locals versus migrants, the latter often excluded from subsidies;
- members of local elites versus ordinary citizens; and
- men versus women, with men often the only member of the pension scheme among the couple.

The new institutional arrangement between pension scheme, villages, and TVE point beyond organized saving. It contains the germs of modern social insurance:

- employers play a role in social security, by paying subsidies;
 - employers make use of the scheme to serve their economic interests; and
 - there are elements of redistribution, organised both by TVEs and villages.
- The system could be developed toward social insurance by standardization, strengthening of rules, definition of standards, and more transparent redistribution.

d. The Economic and Political Environment of Pension Schemes

This section focuses on two questions.

- What is a favorable environment for pensions? What economic, social, and political conditions have to be met for pension schemes to operate smoothly?

- And vice versa: What effects on their environment do pension schemes have? Do some schemes have negative effects, e.g., on the economy, or maybe even positive effects? This will depend on the design of the scheme.

Three environments are of particular importance: the economy, individual behavior patterns, and government policies. All three are precarious in the PRC and account for the difficulties in spreading rural pensions.

Economic conditions: The state of the local economy is obviously a prime condition for the creation and the sound operation of a pension scheme. The basic dilemma is that in areas with most poor people there tends to be least government revenue to meet those needs.

However, very poor people may be included formally in a general old-age security system that would include subsidies from government and, through pooling, from better-off areas to allow very low basic benefits. The minimum living standard system may also be applied. Inclusion in some national scheme would at least symbolize that they have not been forgotten—that they are recognized, if on a low level, as citizens of the PRC.

Rich areas can take the lead in the first stage while poor areas can be included symbolically. The rich areas would include the well-off coastal provincial units Beijing, Tianjin, Hebei, Liaoning, Shandong, Shanghai, Jiangsu, Zhejiang, Fujian, and Guangdong.

Behaviour: Also, people with a fairly low income often could pay contributions (or pay more than they actually do) but they may have alternative preferences. In our interviews we came across a broad range of spending items that were competing with contributions for old-age pensions. Spending money on medical services in case of ill health of a member of the family or providing for such cases is a paramount concern of all our interviewees. Since medical services have to be paid for, "medical impoverishment" is a constant threat to many people.

Paying for education is another item. Even if formal schooling is free for a certain number of years, there are expenses like books, special charges or, in case of remote areas, accommodation. Education, too, has a high priority in people's budget but it is often very difficult to afford.

Government policy: There are three fields of policy which impinge on rural pensions schemes:

- health policy and educational policy,
- central policy toward old-age security, and
- agricultural policy.

The two first are putting rural pensions under pressure right now, whereas the third field, agricultural policy, is a more general context of pensions that is likely to become immediately relevant only in the near future.

Health and educational policies are relevant for the reasons just given. Most officials said that 80% of poverty was caused by illness, a figure issued by MOCA.

Central policy toward old-age security: As mentioned earlier, the recent loss of trust in the pension scheme is largely caused by a lack of support from the center. This we found in all

counties visited. The first critical event was the transfer in 1998 of the pension administration from MOCA to the Ministry of Labour and Social Security (MOLSS) at all levels of government (though not in every part of the country). The second critical event was the signal given by the central government in 1999 that the scheme should be stopped. The administrators we interviewed at the county, town, and village levels called for a signal by central government to show commitment to rural pensions, including

- passing a law on rural pensions,
- making participation compulsory,
- giving subsidies,
- granting tax deductions for contributions, and
- resuming active campaign for pensions in the countryside.

Agricultural policy. The future of rural social security is linked to agricultural policy in three ways.

- With the increase of marketization and the decrease of the social security function of land, the need for a modern formal social security becomes more urgent.
- By limiting the commercialization of agriculture, the PRC Government currently reduces the need for a formal arrangement for old age. Although the use of land for subsistence is already eroding, land can still be referred to in political rhetorics.
- When a full commercialization of agriculture will be on the political agenda, old-age pensions and other social policy measures can be used to support and accelerate the change, following up on European experience.

e. Is There a Case for Commercial Provision?

In the debate about the future of the rural pilot pension scheme, the idea of letting commercial insurance take over the scheme has come up over the last 2 years. This debate needs clarification. "Going commercial" in old-age security can mean something very different.

- It can simply mean government inactivity: Letting anybody take up commercial insurance or private pension plans if he or she can. Government would neither care for those who cannot, nor seek to regulate the market for private pensions. This is passive commercialization.
- It can mean an active policy of creating a market for financial services and commercial providers, by comprehensive regulation (active commercialization).
- Commercial elements can be restricted to the management of funds of public schemes.

In rural areas, commercial provision as well as public-private partnerships are not new. Right from the start in 1991, the public pilot schemes faced competition by commercial insurance companies. There were also partnerships between the state family planning agencies and commercial insurance.

The assessment of these previous experiences as well as the estimate made on the basis of the current operation of commercial companies do not suggest that commercial providers could take a substantial role in rural old-age security.

- Due to increasing competition in the life insurance market in recent years, most insurers shifted their focus to the urban areas. The rural market is not very profitable.
- It would be expensive for farmers to participate in commercial insurance schemes due to high administrative cost.

- With regard to a takeover of the MOCA/MOLSS schemes, the commercial companies are worried about the financial situation of these schemes (both liabilities and assets) and about possible further state intervention.

If commercial solutions should be adopted, sound regulation would be needed. While government agencies focus on the supply side, on regulating corporate actors and market transactions between them, the regulation of the demand side, that is consumer protection, should also be secured, especially for less educated groups like farmers. Clients need assistance and protection vis-à-vis large-scale corporations. This is the social side of regulation that ought to supplement the economic and financial side.

Scandals about false selling of pension plans to consumers are familiar in Western countries, and they have caused considerable trouble for the government. The PRC could learn from the forms of regulation developed in these countries in response to such scandals.

7. Policy Perspectives

a. Designing Pensions for Rural PRC: Principles and Options

The following principles of reform have emerged from this study.

- **Base entitlements on employment whenever there is an employer.** This principle reacts to the rural industrialization and it can be useful both for employees and employers
- **Make participation in the scheme compulsory,** at least for designated groups. This will make full use of the ability to pay of many persons who otherwise would not join although they could. Compulsory membership also provides a basis for pooling and redistribution. Further, it may reduce the gender bias in participation—found, e.g., in the current rural pilot schemes. Compulsion will also reduce the need for social assistance by guiding people to take a long view of their lives and provide for themselves through contributory schemes.
- **Elements of social redistribution are inevitable.** As experienced in all European countries—rich or poor, recently, or at an equally early stage as the PRC—farmers are a poorer section of society that cannot fully provide for themselves (see Chapter 4.D). Pooling state subsidies and tax deductions for contributions to public and commercial schemes are key instruments.
- Pension reform is more than reforming pensions: An **integrated reform of old-age security** also has to consider the various need-based systems (social assistance) and merit-based systems (pensions for cadres, civil servants, and servicemen). All of them cater for the elderly and all will have to cope with the ageing of the population. Morally, ageing and unemployment are problems of society at large and the ensuing burdens should not be put only on the shoulders of urban workers and farmers and their respective pension schemes.
- **Take a national view beyond the rural-urban divide.** First, the category "rural" is no longer suited as a basis of pension reform due to the rise of rural industry and migration. Many farmers do not work in the agriculture sector. Second, rural and urban areas are increasingly linked, through migration and urban pension entitlements in some rural TVEs. This poses problems of compatibility of security systems and of transfer of entitlements. Third, current financial demands made by the urban pension system toward the proceeds from state asset sales raise moral questions of a just distribution of resources in the PRC society.

Five options are discussed: a no-pension policy; a scheme linked to family planning and confined to one-child families; an extension of the current pilot schemes; a dualist social insurance; and commercial provisions. Except the fourth one, which derives from European experience with rural pensions, all of them figure in the current debate.

Option 1: A No-Pension Policy (passive commercialization)

The nondecision about the future of rural old-age security since 1997 amounts to a non-pension policy. However, a nondecision is also a decision. It does not leave the future open. First, a pension scheme already exists in the countryside. The inaction by the Government, the lack of support, has seriously damaged the scheme. Second, inaction is an implicit decision in favor of commercial schemes. It is a kind of "passive commercialization," which means letting anybody take up commercial insurance or private pensions if he or she can. Government would neither care for those who cannot, nor seek to regulate the private pension market.

Option 2: Pensions for One-Child and Two-Daughter Families

This scheme has been devised and would be run by the State Family Planning Commission (see Chapter 2 B). In this way it is partially a nonpension policy like Model 1. It is restricted to a certain group and aims primarily at rewarding a certain generative behavior rather than security in old age. However, the State Family Planning Commission (SFPC) scheme might also be a pragmatic starting point that could grow into something bigger, a social insurance with wider coverage.

Option 3: Extending the MOCA/MOLSS Pilot Schemes

It is a system of organized saving. On the one hand, this is an achievement in a developing country. On the other, when planning for the future, this will not do. A substantial development would have to take it toward social insurance (option 4), by introducing defined benefits or defined contributions, redistribution (to replace and extend the current hidden forms of redistribution), and subsidies (to replace and standardize the current disorganized system of local subsidies). In richer areas, subsidies from various levels of government seem to be feasible financially.

Option 4: A Dualistic Social Insurance

The rural population could not be covered by a "normal" social insurance scheme that treats participants basically as equals and provides benefits that account for a substantial, if not the biggest part of income in old age. This, however, does not imply to exclude the poorer sections. They could be integrated in a scheme that formally extends to all citizens but is divided in two parts, a dualistic structure. In this way a framework for undivided citizenship would be created that could grow tighter over time.

The primary, employment-based segment would be closer to social insurance as found in the urban sector or in Western countries. It would cover all people employed in rural areas basically TVE employees. Well-off agricultural farmers could join on a voluntary basis, on similar terms as the urban self-employed who are included in the urban workers pension scheme.

The secondary, farming-based segment would be confined to real farmers who mainly earn their living through land use. This part would still have basic characteristics of social insurance, like contributions paid by participants and, to a degree, earnings-related benefits. It would not be tax-financed social assistance, but would rely on heavy subsidies from the Government.

This dual structure is the model adopted by most European countries for their farming population. Only the universalist schemes in the Scandinavian countries have chosen a unified approach. Different versions can be found in Europe, ranging from separate schemes for farmers to separate rules for farmers within more encompassing schemes. Over time, the secondary segment could gradually adopt similar benefits.

Option 5: Commercial Provision

Coverage of commercial provision in rural areas is limited and requires massive state subsidies just as public schemes. Still, it might be one component of a broader welfare mix for better-off people.

Should this option be chosen, several problems would have to be dealt with. First, the Government should pursue by comprehensive regulation an active commercialization to create a sound market for financial services and commercial providers by. Second, supplementary public schemes would be needed to provide for gaps due to small insurance contracts or to a general devaluation of assets during a crisis of the financial markets. Third, should the Government seek to enter a public-commercial partnership, it should resist the temptation so common in the PRC to build on a supply monopoly.

b. Supporting Benefits and Services

In this section we look at essential social benefits and services outside the field of pension, including

- medical services and education,
- advisory services and counseling for farmers,
- social reporting and monitoring in the field of pensions and the living situation of the elderly as an instrument of social planning, and
- the Minimum Living Standard System (MLSS).

The last type of support measure is relevant to pensions in three ways:

- The traditional forms of social assistance in the PRC at the village level—Five Guarantees, Poor Relief, Disaster Relief—also cater for the elderly, the Five Guarantees scheme even almost exclusively. From 1996 the MLSS has been extended to some rural areas, and many of its beneficiaries are old people. For many elderly, probably for most, social assistance is the only benefit they get.
- Social assistance may also be paid to recipients of pensions when pensions are too low. In all Western welfare states some kind of social assistance is provided to supplement social insurance.
- Developed forms of social assistance like the MLSS could also be conceived as the main provision for old age, as an alternative to pensions. A special social assistance scheme with

flat-rate benefits was announced in 1995 by the Indian Government. The introduction of the MLSS is a major departure in social policy, a step towards a modern welfare state.

c. A National Scheme?

In this section we argue that the question "unified or separate" is secondary to the question on which principles the two systems should be based and how they should or could be linked. Depending on the arrangement this might still be called a national system. Unification in this view is only one form of coordinating rural and urban pensions.

Why a national or nationally coordinated scheme? Three reasons can be given:

- labor mobility,
- erosion of the distinction rural versus urban as a basis of eligibility to pensions due to TVEs and migration, and
- questions of equity between different parts of the population.

There are basically four models of national coordination.

- Unification: This is no option, at least not in the foreseeable future, because the systems differ too much and the urban system is in disarray.
- TVE employees could be included in the urban scheme.
- Following some European examples, farmers could be included in an encompassing scheme but be subjected to special regulations with reduced entitlements.
- The systems could remain separate but build up similar structures with a view toward convergence over time. The German systems for blue-collar workers (founded in 1891) and for white-collar workers (founded in 1911) could serve as an example.

In each case the crucial question is how the two parts are linked and coordinated. Three problems have to be solved: how to transfer individual entitlements between the parts; how to subsidize the poorer segment of the system, by state subsidies and/or by redistribution among the members of the overall system through pooling of funds; and how to deal with questions of equity that arise from a structural asymmetry. The inclusion of TVE employees and migration to cities will strengthen the employment-based segment but will weaken the farming-based segment part. The current plans to use proceeds from state assets sales to relieve the urban pension system raises similar questions of equity.

d. Conclusion: Is There a Case for Public Pensions in the Rural PRC? From Land Reform to Globalization

This report, based on existing research and field visits in rich and poor counties, could refute or at least qualify most of the objections against rural pensions: It is not too early, judged by the experience of European countries many of which introduced pensions for farmers at similarly low or even much lower levels of economic development than the present-day PRC. The traditional support systems still do a job but they are increasingly weakened. The industrialization and modernization of the countryside reduces the role of land in the rural economy and in the life plans of the rural citizens. The pilot pension schemes have successfully introduced the idea of organized individual provision for old age, though in the simple form of organized saving with low benefits and a limited number of participants.

The absence of a major economic rationale may account for the persistent disinterest of the central leadership in farmers' pensions.

The use of land as a social security system for farmers limits the commercialization of agriculture. When agricultural commercialization is put on the agenda of the Government, the introduction of old-age security will be as important as urban pension reform is today for the commercialization of urban enterprises. In European countries, old-age security for farmers has acted as a major force of accelerating the transformation and reduction of agriculture. This need could arise in the PRC in the near future.

The fear that rural pensions might be risky is not unwarranted. In all Western welfare states, public provisions, once established, showed a tendency to grow and to absorb more and more state revenue (or contributions from wages). However, no country—not even the United States, if on a lower level—has escaped this momentum.

8. A Plan for Action: Filling the Social Security Gap for the Rural Elderly

a. Problems and a Solution

Figure 8.1, a "problem tree," summarizes the problems of old-age security in the rural PRC.

The key finding is that there is an institutional vacuum: The traditional arrangements for old age, namely family support and land use, are increasingly outlived. At the same time, new structures like the MOLSS pilot schemes and commercial insurance are little developed as yet. This creates a gap between eroding traditional arrangement for old age and underdeveloped modern ones.

The thrust of the report is that there is a case for public pensions in the rural PRC: pensions are both needed and possible. However, the huge economic differences between different areas must be taken into account. Therefore, setting up different models for different areas, according to the status of the area (rich, middle, poor) is proposed and this is summarized in Figure 8.2.

- For poor areas, a specific old-age pension is not proposed, but rather to rely on traditional antipoverty policies. Supplementary measures beyond income maintenance like free or low-cost health care should be a priority. They are affordable by local governments and symbolize a commitment of Government to the citizens concerned.
- For middle areas, the urban MLSS should be spread to rural areas in addition to the measures proposed for poor areas.
- Only for rich areas is a full-fledged modern social insurance is proposed. The details of this kind of social insurance are outlined in Figure 8.3, an "objective tree."

Commercial insurance would have to solve the same problems as a public scheme and would have to provide alternative solutions for each of them. Benefits from public sources will be part of a wider welfare mix, including (reduced) family support, land use for subsistence, and commercial insurance.

b. Practical Steps

1. Timing: Introduce Old-Age Pensions Stepwise But Pass a Law Now

The first aim is to draft and pass a law as soon as possible and to set up the necessary agencies. No further pilot schemes should be started. A decision symbolizes a commitment of Government. The old-age pensions act to be passed may provide for a stepwise introduction of several components of the scheme.

2. Categorize Areas According to Economic and Administrative Level

To facilitate labor mobility and secure a stable and accountable administration, a higher level of government—either province or municipality—should be chosen. The decision which province or municipality falls under which category—rich, middle, or poor—should be taken jointly with the local governments concerned. It must be open to revision. Areas can be upgraded or, if necessary, downgraded. The rich areas would primarily include the coastal areas in the east.

3. Make Institutional Choices

Great choices like state versus private (in PRC: public versus commercial) or funded pensions versus pay-as-you-go are not as clear as they seem. Each solution has its problems. The following are key areas of choice.

- Public versus commercial
- Funded systems versus pay-as-you-go (PAYG): In funded systems, unlike the PAYG, the profit is only visible to participants some 30 or 40 years later; Getting a funded system started is always a problem (s.b.), while the PAYG can start any time without subsidy.
- Tax deductions: Tax deductions for the elderly should be part of old-age security. They are both feasible (amounting to an estimated 0.25% of government revenue) and morally justifiable because urban pensions are not subject to taxation, while for farmers land acts as social security.
- Redistribution: As in all European countries, massive redistribution is needed for rural pension schemes. For richer areas a subsidy to the contributions paid by the poor would be feasible, accounting for 1% of the budget, as calculated for the Yantai Municipality (to ensure that no citizen falls below the poverty line in old age).
- Benefit standards: Even if benefits are low it is crucial to define standards. Standards may be based on a basket of goods considered to be essential for living or be defined in some other way. Defining standards requires a commitment by the Government to certain goals.
- Coordination of rural and urban schemes: The formal nature of the integration of rural and urban systems is second to the question how well coordinated they are. There is a range of choices like in European countries: separate rural pensions, integration of farmers into more general pension schemes, and inclusion of farmers into a universal scheme that covers the entire population.

The portability of pensions would be enhanced through sound coordination. In this respect the PRC can learn from the countries of the European Union (EU). If different systems are well coordinated, then inclusion of TVE employees in urban pension systems could be an option.

4. Provide Funds to Get the Rural Pension System Started—the Problem of Transition

The transition to a new funded system poses problems. In the current reform of the urban pension scheme, a massive injection of money from selling state-owned enterprises (SOEs) is planned to start the urban system anew.

Morally it would be justifiable to use part of the proceeds of the SOE sales for rural pensions. There is no reason why the total loss of the urban pension funds should be compensated out of national property while rural citizens continue to get no subsidy or even no pension at all. If land should also be privatized in the future, proceeds should partially go to the farmers.

5. Institutionalize Monitoring and Evaluation

The effects of a pension reform should be continuously monitored and evaluated. A board of experts should be set up to produce an annual report. Reports should not be restricted to public pensions but should include general indicators of social security among the elderly. Last but not least, further research into the matter is needed. In contrast to the ADB report on urban pensions, this report on rural pensions rests only on the work of one international expert from one discipline, supported by one domestic expert. A larger research team from several disciplines is needed.

Chapter 1. WHY RURAL PENSIONS? NEED FOR POLITICAL ACTION

The distinction between rural and urban (*nongcun, chengshi*) has been central to the PRC society since 1949. Indeed for all developing countries and in the history of Western countries, this has been a major social dividing line. The relationship between rural and urban areas and the tensions between the two have often acted as a force of social development. In post-1949 PRC, this distinction took on a special shape.

A. Divided Citizenship: The Rural-Urban Divide

The PRC society rests on a notion of divided citizenship. The distinction between rural and urban is politically and legally created and reinforced by a strict separation between two kinds of social organizations and by various checks to migration from the countryside to the cities. First, the rigid system of household registration (*hukou*) allows changes from rural to urban only in a few specified cases. Second, the policy of nontradable land use rights ties rural citizens to their place of origin. Third, when rural citizens try to migrate to cities in spite of these hindrances, they enjoy fewer rights and entitlements to schooling, housing, and other public services as well as to jobs. This has resulted in a delay of urbanization, especially in the prereform era up to 1978 (Table 1). The moral foundation of the rural-urban divide lies in the social contract of the early years of the new PRC. Through land reform farmers received land while urban citizens were given a place in industry coupled with state-provided social security.

Table 1: Urbanization in the PRC
(%)

Year	Total Population (million)	Indicator A (household registration)		Indicator B (administrative organization)			Indicator C (permanent population)	
		Nonagri- cultural	Agricultural	City/Town	City/Town nonagricultural	County	Urban	Rural
1952	575						12.46	87.54
1955	615			15.23		84.77	13.48	86.52
1960	662			24.69		75.31	19.75	80.25
1961	659			22.45	16.10	77.55	19.29	80.71
1970	830			17.38	12.68	82.62	17.38	82.62
1980	987			19.39	14.04	80.61	19.39	80.61
1985	1,059			36.13	16.98	63.87	23.71	76.29
1990	1,143			52.31	19.01	47.69	26.41	73.59
1995	1,211			70.21	22.51	29.79	29.04	70.96
1999	1,259	25.51	74.49	73.00	23.91	27.00	30.89	69.11
2000	1,270							
2005	1,330							

Notes: The new cities and towns, set up since 1984, have a large proportion of agricultural population. Especially in recent years, many townships have been changed into towns and, as a result, town population has sharply increased. Compared with the data before 1984, the proportion of nonagricultural population in cities and towns has become much lower.

Indicator B Definitions: a) *city population*—total population within the jurisdiction of cities (including those living in towns directly under the jurisdiction of cities, excluding those living in counties under the jurisdiction of cities); b) *town population*—total population living in towns under the jurisdiction of counties (excluding those living in the towns directly under the jurisdiction of cities); c) *county population*—total population living in townships under the jurisdiction of counties.

Indicator C Definitions: Urban: a) city population—total population living in districts of cities with district establishment and living in street committees of cities without district establishment; b) town population—total population living in neighborhood committees of towns directly under the jurisdiction of cities without district establishment and living in neighborhood committees of towns directly under the jurisdiction of counties. *Rural:* county population—total population in a given area excluding city and town population.

Source: National Bureau of Statistics (NBS) (2000: Table 4-1); NBS Department of Population, Social, Science and Technology Statistics (2000: Tables 4-5, 4-6, and 5-5).

The organization of social security not only reflects this divide: It is part and parcel of it. Social policy is a major device in constructing and deepening the rural urban divide (Bo 1999). Schooling, housing, and public infrastructure are organized on different base, and there are fundamentally different institutional arrangements in health services and old-age security. Whereas urban citizens enjoy a generous system of old-age pensions introduced early in the 1950s and surpassing the usual standards of developing countries, there are no public provisions for old age in rural areas.

Older people are only entitled to residual forms of public support also accessible to other citizens. These schemes—like Five Guarantees (*wubao*), Poor Relief, and Disaster Relief—are of a premodern poor relief type. They involve means-testing and are restricted to urgent and temporary situations. They are a kind of public charity, not an insurance based on contributions by the beneficiaries. However, being organized by local semigovernment at the village level, they can also be seen as a kind of organized mutual aid. Benefits are low just as the number of recipients.

All in all urban areas have been receiving more attention from the Government. Although the political liberation of the PRC in 1949 originated from the countryside and in the early 1980s the rural areas took the lead in social reform and modernization, the problems of urban areas have been the focus of government activity. This was linked to the buildup of industry, originally following the Soviet model. The urban industrial workers and cadres became the main political basis of the new PRC.

In the field of old-age security, however, after scattered local initiatives in the 1980s, the Ministry of Civil Affairs (MOCA) in 1991 designed a basic framework for public rural pensions, which was tried in the following years in selected pilot areas. In the late 1990s the disparity between rural and urban became apparent again. While urban pension reform figured high on the government agenda, ensuing from the urgent need of reforming state-owned enterprises (SOEs), central decisions about the future of the rural pilot schemes lingered. Indeed this report itself indicates the disparity: The money spent on the report on urban pensions is twenty-five times the sum spent on the rural report. In social science, too, there are much more studies of urban social security than of rural social security, and this applies in particular to pensions.¹

B. Are Rural Pensions Needed at All?

Talking about rural pensions is not talking about reform but about setting up a system where there has been none before. The pilot schemes in various areas cover only some 10% of the rural population. While in the reform of urban pensions their existence is not questioned by anybody, the first question to address in the case of rural pensions is if there is a need for them

¹ For studies of rural social security see e.g. Wong (1998: 93-112), Krieg/Schädler (1995, 2000), Liu (2000) and (Lin 1994)

at all. Before thinking about the most appropriate form of rural old-age pensions, this question deserves close attention.

In the public discourse there is no consensus whether a rural system should be established. First, family support and land are often invoked as a traditional form of support in old age that should continue to play this role in the future. Second, there seems to be no immediate economic pressure comparable with the reform of SOEs in urban areas. On the government agenda, the modernization of the urban economy is not matched by an analogous plan for modernizing the rural economy. That would include reforming the system of state-owned land and creating large-scale agricultural businesses to maximize profit and international competitiveness. Indeed, as we will argue, if such an economic strategy were pursued for rural areas, there were good economic reasons for setting up a rural pension scheme.

The lack of consensus about the need for rural pensions is also at variance with the situation in the field of health services, the other field investigated in this project. While few people would seriously question that there should be public health provision, the need for old-age pensions is contested also among the central political leadership.

In other developing countries, also in transitional economies that are predominantly agrarian, public schemes of old-age security for the rural population are not common at all. Establishing rural pensions is not a self-evident issue. In Western countries, rural citizens were often covered at a late historical stage, either by separate systems or by integration into broader schemes. Support for rural areas has often assumed not the form of social security but of subsidizing and promoting the rural economy. In fact, agriculture has been a troublemaker and major fiscal burden for Western governments till the present day even in the face of a very small proportion of agriculture in the overall economy. By its membership with the World Trade Organisation (WTO), the PRC may also increasingly face such problems.

However, it would be too simple to infer from Western experience that it is too early for the PRC to establish rural pensions. Western research on the development of welfare states has shown that social security systems grow with industrialization and modernization: The more industrialization, urbanization, economic growth, and population ageing, the more society spends on welfare. But different countries have started to set up social security systems at different stages of modernization and have also chosen different system designs.

Modernization in the PRC is unbalanced: In some respects the PRC has reached the middle- or even high-income level; in other respects it is still a developing country. Therefore, there is no clear rule as to what extent and form of social security is appropriate at the current development stage. It is a situation unprecedented in the history of Western societies.

Moreover, countries like the PRC are embarking on setting up social security at a time when many developed countries have already done so and could act as a model. This, too, is different from the situation in which the Western countries found themselves at the onset of social security. In other East and Southeast Asian countries, social security systems have been established at an early stage, compared with Western countries (Hort/Kuhnle 2000). In the PRC, the introduction of the Minimum Living Standard System (MLSS) is a case in point. It is a step toward modern social assistance that comes very early compared with Western societies. It may be concluded that it is not easy to generalize about the right timing of introducing social security schemes.

C. Reasons for Rural Pensions

Nevertheless, there are four major reasons for considering the setting up of old-age pension schemes in rural areas in the PRC:

- the foreseeable ageing of the population,
- socio-economic change in the countryside,
- the long-term character of pension policy, and
- the need for a central political decision after years of uncertainty about the existing pilot schemes

1. Ageing of the Population

There are expectations of an increased future demand for provisions for the elderly, caused by demographic change. Policymakers tend to be shortsighted, but the demographic changes have mobilized a more future-oriented point of view in Western countries as well as in some developing countries. The proportion of elderly in the population is expected to soar and, more specifically relevant for social security, the numerical relation between the number of elderly and the number of middle-aged persons is expected to rise (see Table 6.2 in section 6.1). The scholarly term "demographic ageing" refers to this ratio and not only to the proportion of elderly that is mostly mentioned in public debates in the PRC.

There is a pronounced awareness of demographic changes, and indeed they constitute a huge challenge. However, it is worth noting that the PRC population ages much less than Western populations. For example in 2030 the PRC will have a lower proportion of elderly than Germany has now. The speed of change, too, is fairly high in some Western countries. In rural areas of the PRC, ageing is more pronounced than in urban areas.

In the lives of individuals and families demographic change means a decrease in the number of children. At least in quantitative terms the traditional support of parents in old age is eroding. However, demographic ageing not only results from a decrease in fertility but also from gains in life expectancy. This shows that ageing is to an extent self-produced by politics (Hou 1997). Success in some fields, namely in health policy and in family planning, creates a problem in another field, old-age security. The PRC has entered the so-called demographic transition to low fertility and low mortality that goes along with modernisation at an early stage. Decline in birth rates preceded the one-child-policy.

2. Socioeconomic Changes in the Countryside

Recent changes in economic, social, and political conditions in rural areas over the last 20 years have raised new social questions. They affect both the situation of the elderly and of the middle-aged persons and their capacity and inclination to provide for old age and other contingencies of life. Again, these social problems partially arise from successful modernization policies.

Changes in the organization of the rural economy. While the decline of the collective economy and the rise of the household responsibility system has brought about a substantial increase in incomes and an improvement of living conditions in the countryside, incomes and lives have become more unstable and insecure. People are increasingly subject to the fluctuations of markets and to the imponderability of individual success or failure. This is a challenge for social policy. Enhancing security is, as the term says, a major goal of state-

provided social security. The new organization of the rural economy as well as sectoral changes (see below) also leads to a new division of labor among the sexes. Therefore, new social policies are also gender policies. Security needs may be different for men and women.

Changes in the sectoral structure of the rural economy (Hussain 1999): Over the last 20 years, a silent revolution has taken place in the countryside. Almost one third of the rural workforce is not rural as suggested by the term—working in agriculture on his or her plot of land—but is mainly employed as wage laborer in the local industry. In 1999 less than half of the workforce (47.5%, down by 21% since 1980) worked in agriculture (Table 2). The employees of township and village enterprises (TVEs) mostly retain their piece of land but work on it only besides their waged job or let relatives or other people do it. Close to big cities the majority of farmers work in industries. These "farmers" (with rural *hukou*) live in "villages" that in fact have become parts of towns and cities and no longer look "rural" anymore.

Table 2: The Sectoral Change of the PRC Economy
(%)

Year	Total Workforce (million)	Primary Sector	Agriculture	Secondary Sector	Tertiary Sector
1952	207	83.5		7.4	9.1
1957	238	81.2		9.0	9.8
1962	259	82.1		7.9	9.9
1965	287	81.6		8.4	10.0
1970	344	80.8		10.2	9.0
1980	424	68.7	68.7	18.2	13.1
1985	499	62.4	62.4	20.8	16.8
1990	639	60.1	53.4	21.4	18.5
1995	679	52.2	48.6	23.0	24.8
1999	706	50.1	47.5	23.0	26.9
2000		48.7		23.0	28.3
2005		44.0		23.0	33.0

Source: National Bureau of Statistics (2000: Tables 5-2 and 5-5) and the outline of the 10th Five-Year Plan.

This changes the question of social security. Land is no longer the major source of livelihood for these persons. They have joined the ranks of those who are the classical clientele of social insurance, namely wage laborers. As wage labourers they are subject to the risks of industrial life such as accident, unemployment, illness, and precarious wage in old age. At the same time wages may easily serve as a basis for collecting contributions for social insurance and for defining benefits.

If the distinction between rural and urban has become obsolete, the category "rural pensions" is no longer a useful basis for discussion. When rural and urban, agricultural and industrial (and the service sector) are increasingly intertwined, a comprehensive debate about old-age pensions in the PRC is called for. This does not necessarily imply that a unified national scheme would be the best choice. But it does imply that rural and urban old-age security ought to be discussed together. In 1998 TVE employees outnumbered the employees in SOEs by far (125.4 million versus 90.6 million).

Migration: The rural-urban distinction is further blurred by the marked increase in migration to towns and cities. Migration is often an attempt at overcoming rural poverty and achieving a better living. Even when many migrants remain at the low end of the urban income

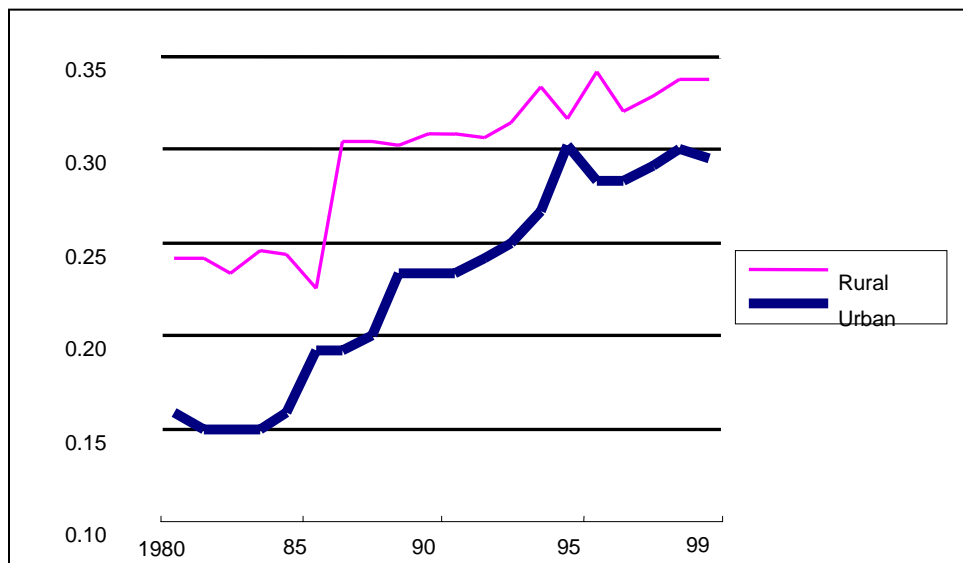
scale, they may still send money home to their families. Traditional ties do not necessarily break but they take on a different shape. This raises new questions of providing for contingencies of life like accident, illness, and old age. To what extent and in which ways do family and land still act as means of support for migrants, which welfare schemes (urban or rural) should they belong to, and how do entitlements travel between different areas and different systems?

Rising incomes and wealth: The PRC has an impressive record of poverty reduction over the last 20 years. This mainly refers to rural areas because before the 1990s poverty was mainly a rural phenomenon. One might infer that there is less need for monetary transfers by government and public benefit schemes. However, this would be jumping to conclusions.

First, poverty is relative. The income gap between rural and urban areas is widening (World Bank 1997). This raises issues of equity. Equity is a major objective and value of state social policy. Measures to reduce inequality might be called for.

Second, inequality within rural areas is also rising. It has always been much higher than inequality in urban areas and still is. As Figure 1 shows, the current debate about excessive inequality in the PRC is fed by rural inequality even more than by urban inequality. Again, this raises issues of equity.

Figure 1: Rising Inequality in Rural and in Urban PRC (Gini coefficients)



0 = Complete Equality, 1 = Complete Inequality

Source: State Statistical Bureau of China (*The Economist*, 31 May 2001)

Third, securing income in old age and reducing poverty are obviously related objectives but they are not identical. It depends on the design of a pension to what extent it contributes to the fight against poverty. Pensions need not only be about reducing poverty. They may also help people above the poverty line to secure and sustain their standard of living in old age. The poverty reduction has become the overarching goal of international developmental policy but other aims like security in old age are also important.

While a decrease in poverty rates may reduce social assistance payments by local governments, increasing incomes, combined with a reduction in the number of children, enable people to join social insurance schemes. Unlike receiving poor relief as a kind of charity, paying contributions to a social insurance scheme is a kind of organized collective self-help. The insured are not paupers dependent on aid by others but self-assured "welfare citizens" who seek security by means of achievement-based social insurance.

Changes in lifestyles: The aforementioned social changes entail new life patterns for the individuals. Life courses become more unstable and varied. This goes along with a change in lifestyle and aspirations of the individuals. People aim at more than daily physical survival. More than before they plan their lives in a long-term perspective, running risks while also seeking security in an unstable world. Besides the quantitative increase in demand for social security caused by demographic change, therefore, there may also be a qualitative increase. Family and kinship relationships also change qualitatively, not only in quantitative terms. To the extent that individuals pursue individual life plans and individual goals, it becomes more difficult for governments to enforce traditional social relations like family support.

3. Pensions Are a Long-Term Issue

In any field of policy making it is wise to prepare for the future. The concept of sustainable development is meant to induce policymakers to think of the long-term consequences of current activity or nonactivity. In the pension field, however, the need for advance planning is paramount.

First, preparation for demographic change—for the ageing of the population—has to start decades before it actually takes place. Unlike general economic development, migration, or changes in lifestyles, future demographic change can be predicted (or more precisely, projected) with a fair degree of certainty.

Second, when individuals plan their lives more than before, then their income situation in old age is a major factor. People who have escaped poverty during working age strive to avoid falling in poverty in old age.

Third, for the operation of pension systems trust by participants is a crucial requisite. Contributors to public pension schemes enter a lifelong commitment. They pay a relevant proportion of their income only to be returned 20–40 years later. Besides the financial obligation they may also build plans for their career, their family, housing, and consumption on the assumption of secure public income in old age. Therefore, they need to be sure about the long-term development of pension schemes. If they remain uncertain about the future development or are even affected by abrupt changes in pension policy, they may easily feel cheated and lose trust in the system. More generally, trust in government is at stake. In Western democracies

pension policy is a major factor of winning or losing elections. We may conclude that pension policy belongs to those fields where we have to prepare for the future now.

4. A political decision by the center is overdue

Whatever one may think about rural pensions—how they should look like and if they are needed at all—a political decision is needed soon. "Experimental policy" by setting up pilot schemes in selected areas is a sound way to promote social reform gradually in a huge society that is in the gear of change. However, there comes a point when the advantages of experimental policy turn into disadvantages. This applies in particular to the field of old-age pensions.

Trust in systems is like a sensitive flower that is difficult to restore once it has been damaged. For some years people have been waiting for a decision if and how the pilot schemes shall be continued or even extended. Millions of participants of the schemes want to know about the future, potential new participants feel insecure, administrative staff is demotivated, and social policymakers are paralyzed. The trust in government by the rural population is at stake. The longer a central decision is delayed, the more difficult it will be to introduce a new system and secure trust for it. A new pilot scheme for urban pensions is about to start. If a coordination of urban and rural reform processes is wanted at all, then now is the time to tackle it.

The conditions for creating a pension scheme for rural areas are favorable since there is no large-scale generous pension system like in urban areas that has to be trimmed down against vested interests and is burdened by a gigantic implicit pension debt. It is an opportunity for setting up a system (almost) from scratch. The slot may close when people can no longer bear the uncertainty and go their own ways in providing for old age.

As experiences in Western countries have shown, the first and basic decision about the structure of a welfare system tends to shape the development of that system for years. Scholars speak of "path dependency," meaning that changes in the system, even in the face of new challenges, depend on the institutional "path" once entered in the beginning. The chance of defining a path opens up only once. This chance has to be seized.

D. The Wider Context: Nation Building and Citizenship

The immediate objective of old-age pensions is to enhance the welfare of individuals. The four reasons given above for considering setting up old-age pensions in rural areas are mainly confined to this immediate objective. However, pensions are more than a device of transferring money to older people. They have wider significance for society, namely:

- to support policies beyond social security, above all economic and family policy,
- to enhance social stability,
- to contribute to the process of institution building, and
- to enrich individual legal rights.

The first function of pensions beyond the immediate welfare aims is to **support other policies** beyond social security. In the PRC, in particular, a major argument for the pilot schemes was to support family planning. The assumption goes that the more people are assured of safe public income the more they may be willing to have fewer children. Pensions

can also support economic growth by investing funds in a fast growing economy that need a capital. This has been a major argument by economists in favor of funded pension systems.

The second wider contribution of pensions to society is to enhance **social stability** and to create citizen loyalty toward government. This is a classical objective of social policy already voiced by Chancellor Bismarck when he pioneered social insurance in Imperial Germany in the 1880s.

Positively speaking, pensions can be a step toward **nation building**, especially in a still young nation like the PRC (Liu 2000). Social security can help unite the country and bridge the division between the "two nations" urban and rural. The term 'two nations' was first used by the British Premier Disraeli in the 19th century when he wanted to point out the dangers of social cleavage and extreme inequality in his country. Michael Harrington made a similar point in 1961 when he referred to the United States (US) poor as "The Other America."

In history, path-breaking welfare reforms have often been linked to crucial stages in the process of nation building. The foundation of modern social insurance by Bismarck was a major component of consolidating the German nation that had been united as a political state only 10 years before social legislation began (unification in 1871, insurance legislation 1883–1889). At that time industrial workers, not farmers, were the main targets of legislation. The foundation of the British "welfare state" in 1945–1948 emerged out of a feeling of national unity during and in the immediate aftermath of the Second World War. The famous Beveridge report that provided the blueprint was published in 1942. The social services set up at the time also included farmers. And even in the US, where the idea of state welfare is least rooted, the depression of the 1930s lead to Roosevelt's "New Deal" of 1935. The name indicates that the introduction of social insurance in that year was more than a new financial arrangement. It was a major component of a new social contract as the basis of a renewed national unity.

Third, setting up rural pensions would be an element of **institution building**. It could imply the creation of new "intermediary" institutions between state and individual. In his famous speech of 1992 Deng Xiaoping had pointed the way toward a socialist market economy. The 1993 and 1999 amendments to the constitution (Liu 1999) reflect this new direction of development. Central state planning and direct control of social and economic relations is to give way to macro control of semi-independent and semi self-regulatory bodies. The renaming of the State Planning Commission as State Development Planning Commission mirrors this change.

The task for government and society is to create and strengthen indirect modes of control like taxation, creating a banking system, developing the stock exchange, and securing independent courts and the rule of law. Socialized old-age pensions separated from SOEs and the newly setup social security agencies are part of this process. These are steps toward a public welfare sector (Kaufmann 1997), a new sector of society that consists of intermediary institutions, which are neither state nor market.

The fourth context of rural pensions is the creation of a legal system that has been going on since 1978. A major aspect of this process is the specification and the guarantee of **individual rights**, above all basic human rights. In the global debate on reforming old-age pensions, the question of extending coverage of existing systems has received much attention. The two major groups named in this context as mostly excluded from social insurance are (overlapping) the poor and the rural population. The International Labour Organization (ILO) sees the extension of coverage as a key aim and basic principle of the idea of social insurance.

This principle can be seen to be founded in law. Most constitutions include nondiscrimination and relief of want among their principles. In the view of J.-V. Gruat (1996) of the International Labour Office, "the extension of the scope of coverage under social insurance mechanisms is just a logical way for the State to fulfil part its constitutional obligations vis-à-vis a wider percentage of the population" (Gillion et al. 2000).

Article 45 of the PRC Constitution stipulates that "each citizen is entitled, in case of old age or when he is suffering a contingency like illness or incapacity to work, to receive material aid by the state and society. The state shall develop the necessary system of social insurance, a system of social assistance and a health system." This implies that this constitutes an individual right, not just an institutional obligation to help (cf. Liu 1999; Wang 1996). The PRC labor law, by contrast, only refers to social security for people employed by enterprises. Article 45 of the constitution clearly goes beyond these narrow confines.

This leads back to the question of nation building. Thomas Humphrey Marshall, the most influential early thinker of the welfare state, has developed a notion of citizenship that comprises three strands: civil rights, political rights, and social rights. Only the combination of the three constitutes full citizenship. Marshall developed his idea in a famous speech delivered in 1949 when looking back on the foundation of the British welfare state that had just been achieved during the three years before (Marshall 1950). The consolidation and extension of social rights through the creation of the welfare state, in Marshall's view, added the third element to citizenship.

The PRC has made progress in establishing civil and political rights. Civil rights have been promoted in the course of economic liberalization since the 1980s, and on the village level grassroots democracy has been emerging since 1988, rekindled in 1998. However, social rights for a wider section of the population, indeed for the majority, remain a challenge. Following Marshall, only by extending the coverage of social security could the urban-rural divide be overcome and full and equal citizenship be established.

For good economic and fiscal reasons recent PRC governments have been cautious when it comes to the expansion of social spending and legal commitments to wide-ranging entitlements to social benefits and services. This report, therefore, also has to examine the economic effects—risks as well as potential gains—of extending public old-age security.

Chapter 2. PUBLIC PENSION POLICY IN THE PRC SINCE 1949— A CHANGING SOCIAL CONTRACT

The PRC pension system and pension policy falls into three almost entirely unrelated parts:

- a system for urban enterprise workers;
- a system for the rural population; and
- a system for public sector personnel such as cadres, civil servants, and servicemen.

The three components have totally different institutions, benefits, and finance; are operated by different departments and sections of government; and were established at different times. Therefore there are three histories of public pensions in the PRC that have rarely touched each other. This tripartite division expresses a basic social contract of the PRC society about the rights and duties of different groups in society. The contract emerged in the specific historical situation of liberation in the late 1940s and early 1950s.

The following account traces the history of the pension schemes for urban workers and for the rural population (section A) and the recent challenge to the underlying social contract (sections B and C). The chapter does not deal with the provisions for public sector employees that are much less researched. A political analysis of the full tripartite structure, however, is given in Chapter 3.

A. Rural and Urban Pensions Policy Till 1997

This section describes the origin and development of pensions policy in the rural PRC since the early 1980s, along with the much longer history of urban pensions, which have accompanied the new republic. The account is divided into four parts. The first one is concerned with the social security provisions available to older people under the command economy. The following three describe the major developments of the pension policy in the 1980s, the early 1990s, and the middle of the 1990s.

1. The Pre-Reform Era (till c. 1980)

On the eve of the new PRC when a provisional Constitution was being drafted, **Chairman Mao Zedong** proposed the introduction of a labor insurance system in the whole country. Since the farmers had got the land after the liberation, Mao argued, the urban workers should also benefit from the victory of the revolution. This was a **social contract** that laid the foundation of the PRC social security system.

Although there were no conditions for a substantial increase in wages and a decrease in work hours, he further argued, it was possible to help the staff and workers in urban areas when they were pregnant, old, sick, dead, injured, and disabled following the example of the successful pilot schemes in the northeast of the PRC. The Central Commission of the Chinese Communist Party (CCCCP) agreed with Mao. Then the 1949 provisional constitution stipulated that the labor insurance system should be introduced in enterprises step by step.

a. Urban: Public Pensions as Part of Nation Building

According to the stipulation of the Constitution, the State Council (SC) under Premier Zhou Enlai ordered the Ministry of Labour (MOL) and the All-China Federation of Trade Unions (ACFTU) to be responsible for drafting the Regulation on Labour Insurance.

The regulation summarized the experience of the CCP, which had not only declared its intention but also taken concrete steps to honor its past pledges in the field of social welfare. Mao, like Lenin, as Fisher once noted, "was in a big hurry to tell the people what the new power was, what it was after, and how it intended to accomplish its aims."

The 1951 Regulation on Labour Insurance introduced not only cash benefits including an old-age allowance, disability and survivor benefits as well as other social insurance benefits, but also benefits-in-kind such as health care and institutional care facilities for enterprise staff and workers.

As for the long-term cash benefits, until well into the middle of the 1980s, it was up to individual government organizations and public enterprises to provide pensions for their own retirees, respectively. From the 1951 regulation on labor insurance till the 1978 regulation on retirement pensions, the initial pensions were determined primarily by the length of service and the wage of the final month, and the pensions were rarely adjusted on an ad hoc basis against the rise in prices.

Since the 1978 regulation is still valid in a sense, it is worthwhile to review the changes it brought compared with previous regulations. In the middle of 1978, the SC sent a circular (SC Document 104 of 1978) including two separate pension regulations for cadres or staff and workers of SOEs, respectively.

The regulation of 1978 not only reinstated retirement, but also provided generous incentives for early retirement. This was done partly to make way for the returning young people who were sent to the countryside to receive re-education from farmers during the Cultural Revolution; and partly to cleanse the ranks of party cadres and government officials. The minimum years of service required to qualify for retirement pensions were lowered to 10, and benefits were raised to make retirement more attractive. Moreover, for a time, workers who retired were guaranteed a job for one child of theirs when there were difficulties with the families.

Given these material incentives, plus political education to persuade older cadres as well as workers obeying the arrangements of the Party for them, the number of retirees jumped fourfold between 1978 and 1985, and pension costs rose from 2.8% of the urban wage bill to 10.6% (calculated according to NBS 1996: Tables 10-1 and 10-17). In 1952 and 1956 there were 20,000 and 63,000 pensioners in total, respectively. Ten years later, in 1966, it was only one million.

b. Rural: Land and Family as Old-Age Security

In the rural area, circumstances were quite different. The social protection focused only on the Five-Guarantee households, poverty-stricken households, and, to a limited extent, retirees. The state also provided rural households with disaster and poor relief.

In addition, old-age support schemes, following the urban model, were introduced in some rich areas to provide old-age allowances to retired TVE workers and rural cadres at the grass roots. The Regulation on the Working of the People's Communes in Rural Areas, approved at the 1978 Plenary Session of the CCP, provided policy basis for such initiatives. It stipulated that a basic accounting unit such as a production group in a good financial situation could provide old-age benefits for its members. According to this legislation, some *xiang* (towns) and *cun* (villages)² voluntarily started to try out old-age support schemes that more or less followed the urban model. It was reported (Dangdai Zhongguo 1987) that those formal arrangements covered a working population of about 200,000 in some rural areas of 7–8 provinces by the end of 1980.

2. The 1980s

In the first 10 years of reforms in the PRC dramatic socioeconomic and political changes posed challenges to the existing old-age support system in both the rural and urban sectors.

a. Rural: First Departures

The major changes in rural areas were

- rapid ageing, partially due to family planning;
- weakening collective economy following the household responsibility system;
- declining regulatory power at the grassroots level;
- liberalization of the household registration system; and
- changing social values.

Under such dramatically changing circumstances, it would be rather risky for a growing number of older people to still rely heavily on a decreasing percentage of younger people with declining moral values, who are more likely to work and even live far from their parents and are increasingly exposed to market risks with little insurance. Therefore, alternative arrangements of old-age support would become necessary for many of older people in the future when they are too old to take care of themselves.

Apart from the demand for alternative old-age arrangements, economic conditions in many areas were also quite supportive. Since the rural economic reform commenced following the Third Plenary Session of the Eleventh Congress of the CCP at the end of 1978, the rural economy had developed rapidly and steadily, and industry and sidelines had become increasingly important. As a result, per capita income increased substantially. The improved financial situation of rural communities in some developed areas produced the necessary economic basis for the introduction of formal pension arrangements. In Easton's (1965) terms, thus, there had been growing stress caused by both demand and support from the below.

Without prompt authoritative instructions from the Centre, however, local governments at grass-roots level and administrative villages responded to growing stress by introducing similar old-age schemes for farmers as the urban system. By the end of 1984, 1,330 townships and towns (2.4% of the total) and 9,410 villages (0.9% of the total) introduced the retirement pension

² Below the county level the former commune has been replaced by the administrative unit called the *xiang* or town, generally, the name depending on the proportion of nonagricultural population or production in this territory. A *xiang* or town usually consists of a number of administrative villages (*cun*). These *cun* commonly have a number of production groups (*zu*), which were production teams under the command economy.

schemes, which were paying out pensions for more than 660,000 people. These statistics might exaggerate the actual progress, but reflected the fact that old-age benefit schemes proliferated over the first half of the 1980s.

According to the recommendations of the seventh FYP concerning the social security system, the SC (Social Security Bulletin, 20/03/1987) in early 1987 approved the Ministry of Civil Affairs (MOCA) to lead the experiments with social security system in the rural sector. To promote the pilot schemes for the rural social security system at the grassroots level, MOCA proposed six models in five provinces for rural social security system for older farmers (MOCA Project Group, 1987: 500-502).

Under the guidance of civil affairs authorities at various levels, according to Zhang (1991), more than 8,000 villages (0.8% of the total), 800 townships and towns (1.4% of the total), and 190 counties (9% of the total) in 19 provinces participated in efforts for some sort of formal old-age arrangements by the middle of 1989.

b. Urban: SOE Restructuring Triggers Pension Reform

Like the Third Plenum of the Eleventh Central Committee, which initiated the agricultural reform, the Third Plenum of the Twelfth Central Committee in October 1984 formally initiated the urban industrial reforms. Moreover, it claimed that socialism would be a planned commodity economy on the basis of common ownership. In addition, the Thirteenth Congress of the Party in 1985 recommended that both planning and market mechanisms cover the whole society. In such a broad context, the Seventh FYP (1986–1990) proposed to establish an embryonic form of social security system in the PRC in the next five years. This was the first time for the term social security to be adopted at such a top level, which was defined to include four programs, i.e., social insurance, social relief, social welfare, and special benefits for current- and ex-service persons.

The economic restructuring program in the urban sector was characterized by reforms to increase SOE autonomy and to encourage the development of the nonstate sector. The reform program of SOEs in the PRC was intended to achieve two main objectives: first, to increase enterprise autonomy and thereby improve performance of industrial SOEs; and second, to modify state ownership itself in order to create and diffuse new forms of ownership. We can broadly associate the two objectives respectively with an initial period of reform, from 1978 to 1988, and a second phase, which started in 1988 and accelerated in 1993.

The following reforms of the urban enterprise pension system had been conducted correspondingly since the middle of the 1980s.

- First, the existing system at the beginning of 1980s, defined by the 1978 regulation, mainly suited the needs of permanent workers in the SOEs. The People's Insurance Corporation of China (PICC) was encouraged to provide pilot pension schemes for the collectively owned enterprise (COE) employees.
- Second, the existing system was provided and financed by individual enterprises without direct, if any, redistribution among enterprises. Moreover, individual workers did not make any contributions to the program. The SC Document 77 in the late 1986 recommended pooling of the pension costs across SOEs on a limited basis, predominantly at the county/city level, and less importantly by certain industrial sectors on a national basis such as the non-ferrous industry and the coal industry. In the late 1980s, pooling was extended to

COE workers in many cities, although these pools were generally separate from those for SOE workers.

3. The Early 1990s

a. Rural: The Breakthrough—Pilot Pension Schemes Set Up by the Central Government

At the beginning of the 1990s, the outline of the 8th FYP argued for not only the necessity but also the urgency to develop a solid and adequate social security system. It was assumed that a complete social security system could promote the successful operation of economic restructuring and long-term social stability.

MOCA was successful in getting the support of MOL and SCRES to issue a joint document on the division of responsibility between MOL and MOCA in the social insurance field. The joint document (MOCA document [1991] No.9) aimed to clarify the borderline between the urban and rural sectors, which, according to the SC routine meeting, should be the territories of MOL and MOCA, respectively. To fulfil the task approved by the SC leader, MOCA established a Temporary Office for Rural Social Insurance Pensions, a provisional working team for local experiments at the county level, in February 1991.

Major policy aspects of the MOCA original plan included the following.

- The scheme would cover all rural citizens with agricultural *hukou* between 20 and 59 years, regardless of their occupations.
- It would be primarily funded by individual participants, but employers or local communities may subsidize individual contributions. The state would grant tax exemption for any contributions to the plan.
- Personal participants, their employers, or local communities, could choose from a set of contribution rates, according to individual capacities of payment and desires, although the long-term objective would be to secure basic living standards.
- At 60 years, individuals could receive annuities based on their total accumulated funds in personal accounts. The benefit formulas, equalizing the total accumulation at the pensionable age with the total discounted value of future pensions, took into account six factors, which included the monthly, annual, or a lump sum of contributions; years of fund investment; an assumed average return rate of pension funds; the remaining life span of pensioners at pensionable age (preferably 60 years); and a minimum 10-year delivery guarantee for those past the pensionable age.
- In addition, accumulated funds should be primarily invested in special government bonds, if available, and, at the same time, local interests should also be taken into account.

In April 1991, MOCA decided to make its initial experiments in five counties, such as Muping and Zhaoyuan, within the jurisdiction of Weihai and Yantai municipalities in Shandong Province, after consultation with the provincial civil affairs bureau (CAB). The Muping County Government (1991) explained in a MOCA working conference in October that year how to campaign for the pilot scheme in their territory. First, to take full advantage of various mass media including local radio, local television, blackboards and bulletin boards, printed materials, and face-to-face ideological education and persuasion by party members at the grass roots, to eliminate the worries among ordinary farmers. They were worried whether or not the promise could be kept and the savings in the pilot scheme would be better than the deposits in banks.

Second, the majority of party members at the grass roots were asked to take the lead in participating in the new scheme to set an example and encourage ordinary farmers to follow suit. According to the Muping County Government (1991), this was the first time in the last decade that such a propaganda and campaign was launched, probably since the end of the Cultural Revolution.

The same experiment was conducted in the next one and half years on a much larger scale than expected, following the success of the pilot scheme in Shandong Province. In October 1991, 52 counties carried out the experiment. By the middle and the end of 1992, 720 and 1,028 counties were on the MOCA list, excluding those approved by local governments themselves. Over this period, the experiment was successfully conducted in many localities, particularly in all suburban counties of Wuhan Municipality and almost the whole territory of Jiangsu Province.

According to a speech (Zhang 1992) delivered at the MOCA conference on the pension schemes in Wuhan in July 1992, the conflict between the MOCA and commercial insurance companies had been intensifying in the rural sector.³ To deal with the insurance companies and to encourage local incentives, the Wuhan conference decided to further liberalize the basic plan for the rural pension system.

- First, children down to 1 year could be covered by the rural pension schemes on a voluntary basis. If sticking to original age limit, local CABs were concerned that few farmers would need the social rural pension scheme any more in the future because insurance companies were inducing single-child parents to buy pension policies for their babies.
- Second, the pilot schemes could begin with TVE employees in a locality, and expand to ordinary farmers later. If local CABs insisted unification, insurance companies would take over the business for TVEs.
- Third, all accumulated funds would be retained in localities to support local economic development. This liberalization attempted to induce local leadership in promoting local pension schemes.
- Fourth, local CABs at higher levels would have the authority to approve applications and local operational plans at lower levels as long as MOCA was informed.

A large-scale experiment, envisaged by the MOCA Minister (Cui 1992) to cover 100 million farmers with 10 billion yuan of annual contribution incomes after three more years' efforts, had caused concern and debates about both the new program itself, which would be discussed much later, and the ways some local CABs bring farmers into the system. In the middle of 1992, the SC leader who approved the MOCA to experiment the pension scheme at the county level asked the Ministry not to compel farmers to participate in the new pension system.

b. Urban: An Initial Framework Adapting to SOE Reform

The SC resolution on the pension reform of urban enterprise employees (SC Document [1991] No.33) was a summary of good practices and theoretical studies of urban pension policy in the 1980s.

³ See also the interesting empirical evidence in Krieg/Schädler (1995).

- It confirmed the partial-funding principle recommended by MOL. It called for individual contributions by all employees, in addition to enterprise contributions. It also called for an expansion of social pooling.
- Moreover, it was also directed at new plans for pension reform. Particularly, it called for the establishment of three tiers in the pension system, a basic benefit, a supplementary benefit to be provided by enterprises in sound financial conditions, and a benefit based on individual saving.
- The document also authorized MOL to administer the basic pension schemes for all enterprise employees, and, on the other hand, it stipulated that the PICC could carry on the business it had got currently from the market.

However, the most important issue remained. The SC Document failed to address the increasingly outdated formulas for pension calculation. According to the 1978 Regulation, a wage earner's pension benefit was determined by his or her primary pension and ad hoc adjustments for inflation. For most workers, the primary pension was computed according to both their own monthly standard wage as well as length of service. The term "monthly standard wage" was the product of the planned economy, which was only suitable for workers in public work units, such as SOEs and large COEs.

4. The Mid-1990s

a. Rural: Consolidation

The Third Plenum of the 14th Party Congress, held in 1993, broadened the meaning of social security originally defined in 1985. Two more programs were added to the social security system. One was social mutual aid, which mainly referred to the pilot mutual aid insurance schemes initiated by the ACFTU for urban workers; another was self-security from personal savings, which mainly referred to the former MOCA rural pension schemes for farmers.

Thanks to the early efforts with the rural pension schemes, MOCA, particularly its mission for rural pension schemes, survived the government restructuring initiatives passed by the 8th National People's Congress in March 1993, which, according to the MOCA document [1993] No.8 (MOCA 1993), authorized MOCA to retain the responsibility for rural pension system. Under the MOCA organizational plan approved in 1993, a special department could be established in the Ministry for rural social insurance, which would be responsible for not only making legislation and development plan for rural pension program but also enforcing them. In addition, one year later, the Central Institution Committee General Office (1994) authorized MOCA to set up an executive agency for the operational services of rural pension schemes. Local governments at various levels followed suit to establish specific administrative organizations within the CABs.

Table 3 shows that by the end of 1997, 2,008 counties (or cities at the county level), 285 prefectures (or cities at the prefectural level) scattered in almost the whole country, except Tibet had begun the undertaking; and, moreover, more than 57% of townships or towns, almost all counties, a little less than 75% of prefectures and 87.1% of provinces established special administrative organizations at the related levels. There was an administrative system from the bottom to the top by the end of 1997.

Table 3: Administration and Staff for Rural Pensions

		Total	Provincial Level	Prefectural Level	County Level	Township Level
Having started the undertaking	Administrative units	-	30	285	2008	32629
	%	-	96.8	85.0	93.7	69.4
Having set up institutions	Administrative units	-	27	241	2076	26847
	%	-	87.1	71.9	96.9	57.1
Number of staff		38,556	187	781	8801	28787

Sources: MOCA (1998), unpublished statistical tables (Table 1) on the rural old-age pension plan in 1997; and NBS (1998: Table 1-1).

Under such favorable circumstances, the civil affairs authorities at various levels should have promoted a steady progress with the rural pension system, as Cui (1992) expected at the end of 1992. By the end of 1994 (Zhang 1995), however, only 45 million farmers in around 1,000 counties participated in the pension system with 2.8 billion yuan of accumulated funds. And in 1995 (MOCA 1995), only 5 million more farmers participated and around 2.2 billion yuan more money was accumulated in the pension schemes of 1,500 counties.

Table 4 shows the development of rural pension schemes in 1997. The accumulated funds increased 3.3 billion in 1997 and about one third of the increase was from investment incomes rather than from annual contributions of participants. The average contribution level was equivalent to a little more than 3 yuan per month, which was almost the minimum contribution rate set by MOCA. The administrative cost, equivalent to 27.9% of the contribution incomes in 1997, was much higher than the liberalized upper limit set by MOCA in 1993, i.e., 6% of the total contributions collected in the current year. Such a high administration cost could be justified on the grounds of starting costs, but it might be too high.

Table 4: The Operation of the Rural Pension Schemes in 1997
(billion yuan)

Accumulated Funds at the Beginning of 1997	10.76
Contributions	3.23
Contributors	82,802,700
Average Annual Contributions	39.0 (yuan/person)
Investment Returns	1.26
Pensioners	557,900
Average Annual Pensions	573.6 (yuan/person)
Administrative Costs	27.9% of contributions
Net Incomes in 1997	3.27
Accumulated Funds at the End of 1997	14.03

Source: Estimates are based on MOCA unpublished statistical tables (1 and 2) the rural old-age pension plan in 1997.

The only encouraging message we can see from Table 2 was that the average benefit rate was quite high. Annual pension incomes amounting to 573.6 yuan were almost equivalent to average per capita total expenditures on food and clothing of rural households in 1997 (NBS 1998). Those pensioners must have made a lump sum of retro-payment to the pension schemes at a quite high contribution rate. This information could suggest that some rich farmers near pensionable age put their trust in the pension schemes.

There were several reasons for the unsatisfactory progress

- First, as Zhang (1993) points out, the competition or disturbance from insurance companies were not eliminated in many localities and even became stronger in some areas. To deal with this situation, MOCA (1994) decided to increase the pension rates set in early 1992 by 10% at the beginning of 1994.
- Second, in late 1992 some government ministries began to accuse the rural pension schemes for being a burden to farmers.
- Third, the Third Plenum of the 14th Party Congress called for a unified administrative system for social security in the PRC. This sent a clear message to localities that it was just a matter of timing to establish a unified administrative system.
- Last but not least, when calculating inputs and outputs, many localities could not and/or would not like to afford the starting costs of such an undertaking and to sustain an executive agency, which had to be almost entirely financed by the administrative costs, equivalent to 3% of the annual total contributions. Thus, they lost incentive and confidence in this pioneering work.

After almost seven years of operation, we can see from Table 5 the policy changes in the rural pension schemes MOCA had made since 1991. Almost all of these liberalization measures were driven by competition from commercial insurance companies, except the additional payment methods, which were adapted to the income pattern of farmers.

Table 5: The Original Design of Rural Pensions (1991) and Later Changes

	<i>The 1991 Original Design</i>	<i>Later Changes</i>
Coverage	<ul style="list-style-type: none"> ◆ All rural citizens with agricultural <i>hukou</i> between 20 and 59 years 	<ul style="list-style-type: none"> • Babies can be covered. • Special groups can be admitted before universal coverage.
Funding	<ul style="list-style-type: none"> ◆ By individual participants, plus, possibly, subsidies from employers or local communities; tax exemption for contributions ◆ Choice of contribution rates depending on individual capacities and desires 	<ul style="list-style-type: none"> • Prepayment and retro-payment allowed of contributions
Fund investment	<ul style="list-style-type: none"> ◆ Bank deposits and special government bonds ◆ Local interests should also be served ◆ Expected return rate was fixed at 8.8% 	<ul style="list-style-type: none"> • Support local economic development only • Return rates set by MOCA annually, slightly above the

	<i>The 1991 Original Design</i>	<i>Later Changes</i>
	per year	interest rate of bank deposits
Pensionable ages	◆ 60 years (preferentially)	• Can be reduced to 55 or even 50 years
Benefits	<ul style="list-style-type: none"> ◆ Annuities depending on accumulated funds in individual accounts ◆ Minimum 10-years of payment ◆ Return rate of investment assumed 8.8% per year over the annuization period 	• Increased by 10% in 1994
Administrative organisations	<ul style="list-style-type: none"> ◆ MOCA Pensions Department: General guidance and supervision ◆ Provincial or city/county social insurance agencies: Administration of funds and individual accounts ◆ Administrative costs up to 3% of current contributions 	• At the beginning of a pension scheme in a county, an extra 3% allowed for administrative costs

b. Urban: A Further Step to Support SOE Reform

With the development of the market economy in the PRC, there had been more and more people working outside the public sector. Moreover, within the public sector, wage management reforms had increased bonuses and allowances to the extent that the standard wage of SOE workers, on average, made up only about 55% of their total earnings in 1991 (MOL 1994). In this case, the Government had to agree to pay extra-standard pensions (or various allowance and subsidies) to make compensations since 1979.

Furthermore, in some enterprises and localities, with the restoration of social pooling, basing the pension on the final standard wage had proved an incentive for them to jack up the final wage in preparation for retirement. All these compensation measures could have contributed to a very generous benefit level. The national average replacement rate of pensions for new retirees was about 85% of the total earnings at the early 1990s; in some localities, the figure was around 100%. These were much more generous than the 1978 rules suggested.

Obviously, the monthly standard wage was no longer fit for the base for the computation of primary pension in the early 1990s. It was also a common view to introduce into the urban pension scheme a mechanism whereby the benefit was adjusted automatically in response to the rapid change in the cost of living or earnings accompanying the economic reform. The questions remained to be solved were the selection of a particular computation scheme for the primary pension as well as a suitable index for the pension-in-payment.

Although there was a general agreement in the PRC about the structure of pension benefits, which should strike the balance between individual equity and social adequacy, two different plans were proposed at the middle of the 1990s for the primary pension formula: Plan I was a defined-contribution type, and Plan II a defined-benefit type.

Following a much heated debate on the operational plans for the further reform at a national conference at the end of 1994, the SC issued a Circular on Deepening the Reform of

the Pension Insurance System (SC Document 6[1995]) on 1 March 1995. This Circular was quite remarkable in that it suggested expanding the pension schemes to various types of enterprises and employees and "**socialization**," that is to transfer responsibility from enterprises to government agencies. Post offices and banks may assist with payment procedures and the latter would be taken over by community-based organizations.

The goal was to establish a unified pension system by the end of 1999. A major principle was that the state pension scheme should combine social pooling with individual accounts. Although the SC Circular No. 6 called for unification of the pension system by the end of the century, it seemed to have contributed to further fragmentation of the system. By proposing two plans and allowing individual localities and industries to choose between them or any combination of the parameters of the two, it had opened up a "Pandora's Box."

A 1997 SC Document reaffirmed the three-tier pension system including the state pension, the enterprise supplementary benefits, and individual voluntary savings tiers. In addition, it urged local governments to establish an urban social assistance system that provides minimum benefits of subsistence. A unified benefit formula for calculating pensions was set up, which was a compromise plan between Plan I and Plan II. It set a goal to transform occupational pooling into local pooling schemes, preferentially at the provincial level. For details of the program characteristics, see Table 6. Although a step forward, such a new pension scheme would be still far from stable for the following reasons.

- The 1997 SC document set a ceiling on contribution rates for both employers and employees. Currently, the combined contribution rates are higher than 28% in some localities.
- The proposed individual accounts are not fully funded. In many ways, they are still notional accounts (World Bank 1997a, 1996; ADB 2001).
- Besides social pooling and individual account pensions, there would be transitional arrangements for current workers.
- The central-local relations are not well defined in the new pension scheme.

Table 4: The Design of the Pension Scheme for Urban Enterprise Employees

Laws and Directives	1978 Regulation, and 1997 SC Resolution
Coverage	A unified system for SOEs, COEs, private, and foreign-invested enterprises (PRC nationals only); and the self-employed depending on local government regulations
Funding	<p>Insured person: Pillar Ia—None; Pillar Ib—At least 4% of taxable wage in 1997, to gradually rise to 8%.</p> <p>Employer: The combined contributions for Pillar Ia and Pillar Ib—maximum 20% of payroll; if beyond 20%, central permission needed. On paper, the contributions for Pillar Ib—7%, gradually reduced to 3% (so that combined employer and employee contributions total 11% of taxable wage); the contributions for Pillar Ia—the rest of total employer contributions after deducting the contributions to Pillar Ib. In practice, however, employer contributions would be first used to meet the current needs of Pillar Ia rather than as savings in Pillar Ib.</p> <p>Government: Pillars Ia and Ib—central and local government subsidies as needed.</p>
Fund Investment	Government bonds only; return rates credited with individual accounts depending on interest rates of bank deposits
Pensionable Ages	Pillars Ia and Ib—Age 60 for men and professional women, 55 for non-professional salaried women, 50 for other women (or 55 for men and 45 for women, if arduous or unhealthful work) with a minimum 15 years' coverage
Benefits	<p>Pillar Ia: 20% of local average wages of preceding year; none if less than 15 years' contributions</p> <p>Pillar Ib: Monthly, equal to 1/120 of total of employer and employee contributions plus interest determined by local governments annually according to the interest rates of bank deposits; benefits beyond 120 months paid out of Pillar Ia</p> <p>Lump Sum (account balance): If less than 15 years' contributions</p> <p>Transitional Arrangements: For employees whose employment began before introduction of individual accounts</p>
Administrative Organizations	<p>MOL Pensions Department: General guidance and supervision</p> <p>Provincial or City/County Social Insurance Agencies: Administration of Pillars Ia and Ib</p> <p>Delivery of pensions changed from individual enterprises to socialized institutions including social insurance agencies, post offices, and banks</p> <p>Levy of social insurance contributions by social insurance agencies or taxation authorities</p> <p>Pension incomes and expenditures to be administered separately, both through a special fiscal account for social security funds</p>

Notes: Pillar Ia = Social pooling pension; Pillar Ib = Individual account pension.

Source: The related regulations and directives, and SSA (1999: p. 79).

B. The Current Political Impasse

SOE reform was probably the most important agenda item at the 15th Party Congress held in September 1997, which spelled out the exact meaning of *zhua da, fang xiao*, i.e. the principle for the second stage of SOE reform. In his report to the Congress, the General Secretary Jiang Zemin pronounced 'public ownership can and should take diversified forms'. The financial crises in the Asia-Pacific region started in the second half of 1997 have also highlighted the weaknesses of China's financial sector. In view of the reform and bankruptcy of SOEs as well as the associated rising unemployment, the development of a nation-wide social security system guaranteeing a minimum standard of living became essential to political and social stability in the urban sector.

1. Urban: From SOEs to State and Society

Unifying the administration. During the 1998 government institution reform (People's Daily, 10/03/98), based on the principle that rights and responsibilities should be integrated, all functions in the field of social insurance formerly fulfilled by MOCA, MOL, MOP, the Ministry of Health, and a few industrial ministries would be transferred to the MOLSS, the only ministry responsible for social security in the PRC, although currently just for social insurance.

As for the pension system, before this institutional reform there were actually three ministries independently supervising and administering pension schemes for different population groups in the PRC: MOL was responsible for urban pension insurance system of enterprise workers; MOP for that of employees of organizations and institutions; and MOCA for farmers' pensions.

Expanding coverage. At the very beginning of 1999, Premier Zhu Rongji signed an SC order to publicize the Temporary Regulation on the Levy of Social Insurance Contributions. Under the regulation, all urban enterprises and self-financed institutions would be covered. In addition, local governments at the provincial level were authorized to require urban self-employed to participate in pension schemes.

Abolishing industry-based pooling. Although the 1997 SC Resolution recommended the replacement of occupational pooling with provincial pooling as the latter widely developed in the whole country, there was no detailed schedule for this transfer. The Resolution made a compromise decision about occupational schemes. It insisted not to abandon occupational pools until the wide development of provincial pooling throughout the whole country. Unfortunately, harsh reality changed the balance. The SC had to force occupational pools to join local pools to help the latter keep their promises to pensioners and to maintain social stability.

Guaranteeing the delivery of benefits. After a tour to Liaoning Province in early 1999, Premier Zhu thought it was as important to guarantee the delivery of pension benefits as to guarantee the basic living standards for those laid off. According to the circular, pensions due for payment in the future must be paid regularly and those in arrears must be also paid retroactively.

Raising benefits. As both a piece of golden cake from the 50th birthday party of the PRC and a Keynesian economic measure to encourage personal consumption from pensioners, a supposed low-income group, the Government decided to increase pensions by 15% in mid-

1999. Obviously, it would be very difficult for localities to encash the new check written by the Central Government.

2. Rural: The Impact of the Rectification Group on the Insurance Industry

In late 1997, a Rectification Group on the Insurance Industry was set up. Besides commercial insurance products, the MOCA pension schemes for farmers and the ACFTU cooperative schemes for urban employees were also covered by the review. After more than one and half years of debate in the Group, the SC sent a document (SC Document [1999] No. 14) in July 1999 to approve the policy evaluation and recommendations of the Group.

The SC decision. The document suggests that there are no sufficient conditions in rural areas to carry out an extensive social insurance pension scheme, and thus the pension schemes already developed by MOCA be cleared up and rectified.⁴ The schemes in those areas with suitable conditions could be transformed into commercial insurance. Obviously, such a decision shows a dramatic change of the SC in its attitude towards the MOCA pension schemes, which had been quite supportive of MOCA to organize the rural pension schemes from 1991 till the beginning of 1998. However, no rectification plan was universally accepted among the major players in this area over the past two years since the publicity of the SC document, which is supposed to have formally settled the dispute about the rural pension schemes, at least on paper.

The background to the rectification of the MOCA pension schemes

- The Asian financial crisis started in 1997. There were some concerns among the PRC leadership over the widespread financial crisis in the East Asia.
- Two state commissions submitted reports to the leadership. In autumn 1997 the former SPC published a working paper to suggest defining strictly the boundary between social insurance and commercial insurance and preventing the insurance industry from risks. At the end of 1997, the former SCRES also made a report, which suggested that the current rural social pension schemes be developed cautiously.
- It was heard that an SC leader made comments on both reports. The leader maintained that (the insurance industry including the MOCA pension schemes) had been in muddle and thus a rectification plan had to be carefully considered. On the second report, he wrote, it would be very risky for the Government to push through the pension insurance schemes in the rural sector.

The main findings of the Rectification—risks involved in the pension schemes. In April 1998 the Group claimed there were some risks involved in several aspects of the pension schemes

- Risks in benefit payment. The assumed return rate was too high and the funds set aside for meeting accrued liabilities were insufficient.
- Risks in the operation of pension funds.

⁴ It is important to note that the subtitle used in the document for the section concerning rural pensions is "the rectification and standardization of rural old-age pensions," rather than "clearing up and rectifying" used in the main body.

- Misleading information to the farmers. The schemes were presented as social insurance by MOCA. Many localities thus claimed during their campaigns that such schemes would secure the basic living standards of old farmers. Another related criticism was that on one hand the civil affairs authorities usually propagandized to the farmers that their schemes were guaranteed by the Government, while on the other hand, they tried to convince the Centre that their schemes were self-sustained and thus there was no need for the state to take any responsibilities. Some group members argued that the Government, at least, would bear the risk of losing reputation to the farmers if the MOCA schemes failed to keep their promises.
- Compulsory participation or so-called voluntary participation under guidance could create discontent among farmers and thus increase social instability in the countryside. Some local civil affairs authorities even tried to link participation in pension schemes with their mandate in other areas such as marriage registration.

Ensuing debates. The first topic is the necessity of a formal arrangement. Some argue that there has been a growing necessity in the rural sector because of a rapid ageing population and a decreasing family size in the rural sector caused by the family planning policy, rural industrialization, and urbanization. Others, however, maintain that small family size does not necessarily mean a declining capacity of family support. The second concerns the nature of the MOCA pension plan. Some suggested to call it a "rural old-age insurance scheme," others preferred an "old-age arrangement."

Finally, it is about the role of Government. Some suggest that the Government encourage multi-means of economic security such as family support, continuing work, community assistance, and life insurance. Life insurance schemes should be developed in rural areas on a truly voluntary basis and run by commercial insurance companies, although probably supported by preferential tax treatments. The government department, as an intermediate agency, is responsible for selection and appointment of appropriate life insurance. Others, however, argue for the state provision in that the PRC society, like other Eastern Asian countries, has little capacity to take care of themselves.

Nonaction after the SC decision. It has been almost two years since the publicity of the SC Document [1999] No. 14. However, its recommendations concerning the rural pension schemes have not been enforced at all.

On the one hand, the SC leader has been committed to enforcing the recommendations over the past two years. In his speech on 26 May 2000 on the upgrading of the social security system at a faster pace, for example, Premier Zhu attempted to convince the audience to go ahead to rectify the rural pension schemes according to the SC decision. In November 2000 (our interview with MOLSS, 20/04/01), Premier Zhu again gave instructions for rectifying the rural pension schemes.

- The rural conditions are not ripe for the development of social insurance. If things go wrong we will be in big trouble in the future. The decentralized management of pension funds would be very difficult and risky. Therefore, the SC Document decided to stop the development of social insurance in the rural sector. For rich areas, farmers could be guided to take up commercial insurance products.
- The funds already accumulated must be checked carefully and must be administered strictly and safely.

- MOLSS should act immediately to make detailed regulations to enforce the SC Document and to do a good job in the rectification.

However, the enforcement of the SC decision has been much delayed mainly because many issues are still open to debate. The related government ministries could not reach consensus. Moreover, both rectification plans proposed by MOLSS (see below) failed to get sufficient support from the related government ministries and institutions, which will be discussed below. Many financial problems in the rural sector inspired the leadership to rectify the rural pension schemes; ironically, they are also warning of a possible social instability caused by any rectification plans not well prepared.

Delayed action, however, put the benefits of participants and administrative staff in greater danger. Since the late 1997 when MOCA knew their mission for rural pensions would be transferred to MOLSS, the rural pension schemes in most localities have been more or less at a standstill. With little fiscal input, many local executive agencies had to use some accumulated pension funds to maintain themselves as well as to concentrate on internal administration. Moreover, most of local agency staff were seriously demotivated by threats or crises accompanying the development of rural pensions since 1991, which include

- some fierce competition from commercial insurance companies;
- accusations that the contributions to rural pensions are part of farmers' burden;
- an alliance between the government organization for TVEs and commercial insurance companies;
- a partnership between the state family planning authorities and commercial insurers;
- rumours and decision about the transfer of responsibilities for rural pensions; and
- the ongoing rectification.

The MOLSS proposals for implementing the SC decision. After the issue of the 1999 SC Document, MOLSS put forward two plans for rectification. The first one made in 1999 suggested carrying on the current pension schemes in those localities with suitable economic conditions, good administrative teams at the grassroots, and sufficient participants, subject to rectification and standardization. At the same time, it suggested local governments to give back the money already collected to participants in those areas with underdeveloped economies and few participants, who could take up commercial pension products on a voluntary basis. Apparently, such a plan implied that commercialized plans would only apply to poor areas. No doubt, it could not be widely accepted.

The second plan made in 2000 set the guideline for an alternative program, i.e., the related policies should be determined by the state, and the provision of services and products by the market. On the basis of such a principle, MOLSS suggested choosing the China Life Insurance Corporation to set up a special branch to take over both the participants in the former MOCA schemes and the administrative staff, depending on the willingness of current stakeholders. The special branch should operate within the policy framework set by the social security authorities. Although the government ministries and institutions concerned accepted the proposed principle, neither MOF nor the insurance regulator agreed to set up such a new institution. In addition, MOF did not agree to write any supporting policies for the transition and the development of any alternative programs.

The rest of this section reviews the most recent reform ideas.

3. Urban: New Initiatives Toward Perfection?

At the end of 2000, SC issued a document (SC Document [2000] 42) to conduct pilot schemes to perfect the urban social security system in Liaoning Province and some selected areas of other provinces (autonomous regions and municipalities).

Innovations in the social security field. According to the SC document, the social security system covers social insurance, social relief, social welfare, special benefits for former and current servicemen, and social mutual aid. For the first time the Government set a target for public spending on social security, probably only in the urban sector. That is, the governments at various levels are expected to adjust their expenditure structure and to increase gradually the proportion of social security spending in the public expenditure to 15–20%.

Innovations in pensions. The 2000 SC document reaffirmed many policy provisions made in the 1997 SC resolution calling for a unified pension scheme for all enterprise employees and the self-employed. On the other hand, the updated document proposed many new initiatives for upgrading the pension area.

First, on the financing side, the following changes were made:

- The contribution rate of individual employees would be immediately increased to 8% of personal taxable wages, rather than will be gradually achieved in a few years.
- All employer contributions would be put into the social pool. That is to say, no employer contributions would be put into personal accounts any more; and the total contributions credited to personal accounts would be reduced from 11% to 8% of personal taxable wages.
- The social pool could no longer use the accumulated funds in personal accounts.

Second, on the benefit side, the combined replacement rate from the social pool and the individual account is expected to reach 58% for an average employee with 35 years of contributions under the ideal condition that the return rate of pension fund investment is the same as the growth rate of local average wages.

Problems remaining. Although the new initiatives wish to replace the bigger notional personal accounts with a little smaller but real ones, the personal accounts would still be underfunded because the factor for annuitization at retirement would be retained at 1/120, which, as the ADB project report concludes, would be too generous for the total accumulated funds in personal accounts to bear.

4. Rural: New Starting Points? Confusion Lingers

Expanding the coverage of the urban pensions to TVEs. At the end of 2000, the Zhejiang Provincial Government decided to integrate the pension schemes for TVE employees into the urban system within 3–5 years. The local regulation, as a first case at the provincial level, caught the attention of MOLSS, although the idea is not new at all.

"The development of township industries inevitably calls for the establishment of a pension system for their employees," a vice-minister of the Ministry of Labour and Social Security (China Daily, 08/09/1999) said at the seminar cosponsored by the Ministry and the France-based insurer CNP Assurances. The official maintained that the implementation of a modernized pension system for older people could increase the further development of township enterprises. Moreover, TVE workers also face the risks of a market economy, and their rights should also be protected, she added. As many suggested (China Daily 08/09/1999) it would help consolidate the urban pension system, which itself is in serious crisis, as warned by some officials (cited in China Daily 08/04/2000). Moreover, the construction of social security programs for TVE employees is also supposed to help promote the rapid development of small towns and cities.

Piloting social insurance schemes for model parents concerning family planning. At the beginning of 1999, the Guangdong Provincial Government publicized a detailed regulation on pension schemes for single-child and both-daughter parents. According to the regulation drafted by local family planning authorities, every qualified couple could get a minimum 1,000 yuan as lump sum contributions to buy pension products from the China Life Insurance Corporation Guangdong Branch. The cost would be shared by local governments at various levels.

Unlike the local initiatives for TVE employees, local pension schemes targeting those model households concerning family planning were recognized by the Centre. The tenth Five-Year Plan (FYP) passed by the People's Congress in March 2001 recommended conducting social insurance pilot schemes for both single-child and both-daughter parents. The FYP, however, made a big revision to the initiatives of family planning authorities: the commercial pension product in Guangdong was changed into a social insurance scheme.

According to the SFPC estimate (interview, 23/04/01), there have been more than 30 million single-child households, 10 million both-daughter households in the rural sector. Moreover, single-child and both-daughter households annually increase by 3.5 million and 1.0 million, respectively. That is to say, currently, about 17% of rural households (NBS 2000:) are qualified for the proposed social insurance schemes. The new initiative is justified because such families have few children and few laborers available for sufficient old-age support (our interviews with SFPC, 23/04/01).

The most recent policy initiative to develop social insurance schemes for some farmers, however, is contradictory to the current government guideline for the rectification of rural pensions. The current Government has insisted that the former MOCA (or the current MOLSS rural) pension schemes should be commercialized in those areas with suitable conditions on a voluntary basis. Such contradictory statements contribute to the current political deadlock in the rural pensions.

According to the outline of the FYP, the MOLSS officials responsible (our interviews, 20/04/01) could justify their pension schemes for farmers on the grounds of supporting family

planning policies in such areas as the Jiaodong Peninsula, the Shandong Peninsula, the Beijing-Tianjin-Tangshan region, and the Delta of Yangtze River. The rural households in those areas are not only rich but also complied well with the family planning policy (interviews with SFPC, 23/04/01).

On the other hand, however, SFPC (our interviews, 23/04/01), the major initiator of such plans, never agreed to call those compensation plans for model households as social insurance. Therefore, they have been concentrating on developing a partnership with commercial insurance companies, although the outline of the FYP called for pilot schemes along the social insurance line. Once again, a new policy initiative created new confusion among the related stakeholders before being translated into practice. This could be the result of both knowledge gap and departmental interests.

C. Looking Back on 50 Years of Pensions: Development and Rationale

1. Continuities and Discontinuities

The history of pension policy in the PRC records many changes in theory and practice, which have been more rapid or profound in some periods than in others, and have essentially continued or departed from traditional ways of dealing with old-age problems. This section summarizes the dynamic characteristics of the PRC pension system and the rationales for pension development.

Looking back, while there have been many reforms in the PRC's pension system over the past 50 years, there have also been considerable continuity in the policy design. A number of continuities can also be identified with the urban pension system.

- The benefit mixture has been dominated by the state pensions.
- There have been special and separate schemes for different population groups and industries, although a unified system for various types of enterprise employees in urban areas has been pushed through in recent years.
- The pension schemes for enterprise employees are financed on a partial funding basis.
- The normal retirement ages remain the same in laws, while incentives for early retirement have been quite common in practice.
- The policy-making and operational functions have been separated since the very beginning of the pension system.
- Moreover, the urban-rural divide remains in the pension area, if it has not widened.

The important changes in the pension legislation over the past 50 years can be summarized as follows.

- The basic policy objective has shifted from poverty relief in the 1950s to income replacement in the 1990s.
- Individual employees have had to make contributions to the state pension system since the middle of the 1980s.
- The three-tier approach was introduced under the 1991 Regulation.
- Benefits-in-payment have been automatically adjusted according to partial changes in average wages since 1993.
- According to the 1995, 1997 and 2000 SC documents, both benefit payment and personal social services formerly delivered by individual enterprises would be socialized soon.

- The most important change recently is the shift in the way pensions will be computed based on individual accounts and social pooling system.
- The administrative function for all pension schemes has been transferred to MOLSS, the only government ministry for various social insurance programs.

The major policy continuities are individual dominant contributions and full-funded personal accounts. Due to competition, many changes have been made in the **rural pension scheme** over the past 10 years.

- Babies could be covered by the rural pension schemes on a voluntary basis. If sticking to original age limit, local CABs were concerned that few farmers would need the social rural pension scheme any more in the future because insurance companies were inducing single-child parents to buy pension policies for their babies.
- The pilot schemes could begin with the cream of society such as TVE employees in a locality, and expand to ordinary farmers later. If local CABs insisted a single timetable for various occupations, insurance companies would take over the cream of society.
- All accumulated funds would be retained in localities to support local economic development. This liberalization attempted to induce local leadership to promote the development of local pension schemes.
- MOCA began to allow pilot countries to borrow money from their accumulated funds to subsidize their operational costs. Then the administrative cost could be raised from 3% to 6% of annual total contributions.
- Although MOCA urged localities to organize the pilot schemes on a voluntary basis, in practice some local civil affairs branches compelled localities and individuals to participate.

On the basis of the review of previous sections, we can summarize the main income sources of older people in both urban and rural areas over the past 50 years in Table 7.

Table 5: The Contrast in Income Sources of Older People Between the Two Sectors

Before the Communist power	Family support, little investment including land	Family, clan support, limited land
1950s and early 1960s	Poverty-reduction type of retirement benefits, family support	Profitable and more equally allocated land, enforced family support
During the Cultural Revolution	Continuing employment, enterprise-based retirement benefits	Continuing labor, enforced family support
End of the 1970s–middle of the 1980s	Income-replacement type of retirement benefits, enterprise-based	Continuing labor, enforced family support
Middle of the 1980s–beginning of the 1990s	Increasingly secured retirement benefits, re-employment and personal savings	Profitable land and loosened family support
Early 1990s	Less secured retirement benefits, re-employment, self-employment and personal savings and investment	Decreasingly profitable land, loose family support, personal savings and piloting public pension schemes
Since late 1990s	More secured retirement benefits, re-employment, self-employment, personal savings and investment, supplementary benefits	Unprofitable land, loose family support, personal savings and, possibly, commercial pension schemes

In short, after 50 years of evolution the basic objectives of the urban pension system transformed from poverty reduction into income replacement. And, at the same time, the successive governments insisted on playing a residual role, if any, in old-age security for farmers.

a. The Changing PRC Social Contract

The review of pension evolution over the past 50 years revealed a PRC welfare philosophy, at least in the pension area, that is, urban employees deserve social insurance for old-age support, while farmers should rely on land. Chairman Mao allocated land to individual rural households 50 years ago and, at the same time, introduced a moderate pension scheme for urban workers. Half century later, the third generation of leadership still insists that farmers depend on land for economic security.

Such a social contract worked well under a command economy when many urban workers in the key sectors of the economy became "the communist men." After intensive ideological education, they understood the national economic situation and could voluntarily control their unrealistic desires for higher welfare benefits. For example, some workers suggested cutting down pension benefits in 1957 when discussing the government consultation paper on the revision of the urban pension scheme. Due to such communist ideas, the rural-urban gap could be contained to some extent.

Under a market economy, however, more and more people would pay growing attention to their own benefits. It would be very difficult for any governments, regardless of socialist or capitalist ones, to strike a new balance among various groups in a changing context such as ageing and globalization. Most capitalist countries rely on social dialogue to reach consensus on the restructuring pension schemes for various groups. In the PRC, few interest groups are involved in the policy process. Basically, it is up to the Government, as "three representatives," to play fair. If the government is still only reactive to the powerful groups and social reality, the policy-created social inequality in the pension area will remain and the pension system will far from stable.

Difficulties with the state-market partnership are a major source of current problems. In the early 1990s the Centre recommended the establishment of a socialist market economic system in the PRC, which would attempt to mix the planning with the market mechanisms. Almost a decade later it is still hard to imagine a good working relationship between the state and the market in the pension industry. Very few members in the rectification group trusted the life insurance market and the ability of the consumers to make wise choice. In some sense, they did not trust their capacity to regulate the market and to enforce the related regulations.

In addition, the evolution of the rural pension policy shows little team spirit and coordination among different departments as well as few partnerships between the state and the market. Most players wished to draw a crystal clear line around their own territories to defend any invasions. And other departments have no right to intervene in "my" business. If failing to get permission to provide services by themselves, the related ministries would like to choose developing a partnership with the commercial sector rather than other government organizations. As a responsible ministry, MOCA never solicited sufficient support from the related government bodies for rural pensions.

Chapter 3. PROVIDING FOR OLD AGE—WHY AND HOW?

A. Welfare Mix, Not Pure Models

Public welfare benefits are only a fraction of the overall provision for old age. In the rural PRC, for example, family and land are the dominant sources of living for the elderly. In many Western countries the bulk of income in old age stems from public sources but even then, as for other age groups, further income and services are provided by family, neighborhood, informal networks, markets, associations, etc.

Any deliberation about public income schemes, therefore, has to take into account that public schemes are only one element in a more comprehensive "welfare mix" or "mixed production of social welfare" (Pinker 1979, Day 1992, Evers/Olk 1996, Leisering 1996). Cases of an almost monistic provision of welfare are historically rare. Recently one might think of highly collectivized social arrangements, as found in the PRC in the late 1950s or in the early *kibbuzim* in Israel, where children were taken out of their families and raised in separate children's houses.

Public debates are dominated by great alternatives, like family and land versus public provision, or public versus commercial, in the PRC debate on rural pensions; or, in Western societies and in the global social security debate, state versus private. These debates are much simplified. They miss the case that normally different models of provision operate at the same time. There is a welfare mix at the level of society, with certain groups predominantly (but not exclusively) being provided for by certain modes of welfare production, such as the elderly in Western societies by public schemes or the middle aged by the labor market and family. At the level of households and individuals we speak of income packages (Rainwater/Rein and Schwartz 1986), that is, combinations of incomes from several sources. A welfare mix may be politically organized, as in multilayered or multipillar systems of old-age security that comprise, e.g., public, occupational, and private provisions.

There is a second reason why thinking in great alternatives is not instructive: The systems usually referred to are themselves not pure with regard to values and institutional design. They are interlinked with elements of other systems. Family for instance is not only informal because it is legally and publicly framed. The obligation to mutual support within the family is laid down in law and is enforced by courts. The operation of the family is deeply influenced by family planning or, in Western countries, by child allowances and other benefits geared to families with children. Land for farmers is not just soil, but as we will argue in Chapter 5.A, is a publicly created and regulated system of social security for rural areas.

Last but not least, private provisions for old age like life insurance are not purely private because, at least in Western countries, they are heavily subsidized by government through tax deductions, are regulated by complex legal frameworks, and are controlled by supervisory authorities. In a democratic welfare state, which depends on the active consent by its citizens, government assumes an overall responsibility for the welfare of its citizens. In this sense private forms of provision assume a public character. More generally, in modern societies the distinction between public and private is increasingly blurred (Kaufmann 1986).

Nevertheless, great alternatives dominate public discourse. They are often used as ideologies that go along with a different reality. Liberal, noninterventionist ideologies may hide that even in countries like the US there is substantial government interference with the economy, such as huge subsidies to agriculture and an enormous military-industrial complex (Kenneth Galbraith) in which government and big business interests are fused. On the other hand, prophets of egalitarianism and socialism like the former British Labour Party failed to acknowledge that the nationalization of basic industries does not turn a liberal market society into an egalitarian one.

We may conclude that institution building in social policy is not about great choices. "The choice between public and private is affected by political philosophies and by relative governments capabilities of the two sectors.... in some countries the governments may not be trusted, while in others there may be relatively little trust in the private sector institutions" (Gillion et al. 2000). This means, first, that we have to make normative decisions, not to find best solutions. What will be best depends on social values. Second, there is no principle that is generally superior, but solutions have to be found in a pragmatic way, according to circumstances. In developing countries, also in the PRC, for example, both public and commercial institutions have limited control capacities.

Third, we should add to that quote from the International Labour Organization handbook on social security pensions, that the choices to be made are not about great alternatives. The real debate ought to be about how to mix and interlink public and private schemes, formal and informal care. Each form of provision has its strengths and weaknesses. There is state failure just as market failure. One might add family failure and land failure. A workable combination of different forms therefore promises to yield a better outcome. A public-private partnership is called for in many areas.

The PRC is peculiar in this respect because all institutions are more or less imbued by the state. Even commercial insurance is not private as in Western countries but mostly owned by the Government, and core parameters of its business like interest rates and scope of investment of funds are fixed by the Government. The discussion about public pensions versus commercial insurance in the PRC is, to a degree, a discussion about different forms of state provision.

B. Why Public Pensions? Rational and Moral Foundations

What is the rationale of public pensions; what reasons can be given for them; what functions, openly declared or hidden, do they have? The immediate function obviously is to provide a living for the elderly. But there is more to it.

Pensions also have a function for the young and middle aged by giving them a sense of security about their future. Economically, pensions have a saving function: They even out income over time, over the life span.

By introducing a standard age from which benefits can be received, pension systems also create a new phase of life in where full employment and labor may no longer be needed. Retirement as an economically inactive phase of life is an invention of modern society. Scholars speak of the emergence of a modern life course (Kohli 1986). Life course means a social structuration of the life span, linked to expectations and plans by individuals that extend beyond daily concerns to the entire life span. In developing countries the institution of retirement has not

normally emerged and, under circumstances of frequent natural disasters, illness and death, overall life plans do not easily come up.

The period of retirement has become a domain for state and public agencies, even in liberal countries like the US. Old-age pensions have been the core of the expansion of Western welfare states. Besides children, who were the targets of early legislative restrictions on working hours, the elderly were the first addressees of public social policy, the first welfare class. This started with the introduction of old-age insurance in Germany in 1889–1891 by Chancellor Bismarck. In the 20th century, the ageing of the population became the most important single determinant of the growth in welfare state spending because pensions and other services for the elderly absorbed so much money (Wilensky 1975).

There must be strong social forces behind an institution to proliferate in the entire Western world. The rise of public pensions rests on strong interests. Pensions proved to be useful for individuals and for the economy. These are the rational foundation of pensions. Five aims are served by pensions, three of them personal and two of them economic:

- securing one's own future (for the young and middle aged),
- being relieved from the obligations toward the elderly (for the middle aged),
- gaining personal autonomy in old age (for the elderly),
- regulating the labor market, and
- disciplining consumption behavior.

With the rise of the welfare state, pensions also assumed political functions. They became a major base of the legitimacy of government. Pension policy can win elections.

As to the first aim: Modernization weakened traditional forms of security and created new insecurities at the same time. The pursuit of security, therefore, became a key concern for individuals. They had an interest in securing their standard of living over the entire life course. People sought increasingly to plan their lives. The security of pensions may matter more for people than financial returns, as found in a survey on the attitudes of people toward social insurance in early postwar Germany (Kaufmann 1973). Only in the 1990s, with the upsurge in the stock markets, have returns become a prime criterion for people to judge pensions.

The second interest of middle-aged individuals in pension is to be free of obligations toward the elderly. They can live their lives more freely when they do not have to care for their parents (Kohli 1989). This does not mean that they surrender the moral obligation: they only delegate it to the state and pay money for that. Neither does it mean that they break up with their parents. They may have intensive ties with them but they do not normally take over basic provision.

The third interest of individuals in public pensions is the gain in personal autonomy. Having his or her own income, an old person becomes independent of social control exercised by family and kinship members. Social control and interference is the dark side of family ties. Dependency of elderly is a major problem for societies like the PRC, which give priority to family support (see Chapter 6.A).

Besides individual interests, there are strong collective and economic interests that make for public pensions: The fourth use of pensions is to regulate the labour market. Historically the interests of employers and employees converged in this respect (Kaufmann/Leisering 1984):

The employers have an interest in a qualified workforce with up-to-date training and in a regular supply of newly trained workers. The exclusion of workers from the labor market beyond an age of retirement serves this purpose. The employees also have an interest in excluding older workers because this keeps labor scarce, reduces unemployment, and strengthens the bargaining power of the trade unions vis-à-vis the employers. For employers, public pensions also externalize costs, making business more profitable. This is a rationale of the current urban pension reform in the PRC, namely to free the enterprises from social burdens by socializing the administration of pensions. Once introduced, the age of retirement can be lifted or lowered, according to the changing demands of the labor market (Lenhardt/Offe 1984).

The other collective and economic function, the fifth use of pensions, is to promote discipline in consumption behaviour (de Swaan 1988). It may train people in planning their consumption prudently and in a long-term perspective. According to sociologists and social philosophers like Norbert Elias and Michel Foucault, discipline is a major requisite of modernization. Disciplined budgeting reinforces individual responsibility and market values, especially when pension benefits are earnings-related. Secure public provision for old age also makes for social stability since, historically, undesirable forms of nonmarket activity like begging, crime, or vagrancy become less likely (Lenhardt/Offe 1984).

But pensions are not only useful from a rational point of view, serving interests of relevant actors in society; they also have a moral foundation. Pensions may be part of the moral economy (Kohli 1987, 1989) of a society. A study by Kohli for Germany showed that old-age pensions may be experienced by the elderly as a just reward for a life devoted to labor, especially in the case of earnings-related schemes. In this way, pensions may reinforce the legitimacy of the social order of a given society. Pension policy is life course policy: By rewarding a normal (male) biography of full and regular employment it confirms and consolidates the dominant ethic of work and achievement (Leisering/Leibfried 1999). Through the moral justification of the social organization of work and through the demarcation of the limits of work by age thresholds, old-age pensions are a cornerstone of the modern work society.

However, work society and generational contract take on different shapes in different societies. Besides the moral foundation of pensions there is a cultural dimension. The value most associated with pensions—security (Kaufmann 1973)—differs between cultures. In Germany the notion of long-term security is deeply embedded in the collective consciousness and highly valued. This was the background of the great pensions reform of 1957, which laid the foundation for the current system. In the first half of the 20th century the Germans experienced twice the extinction of funds accumulated for old age through war and postwar hyperinflation. As a consequence security of pensions, not financial returns, became their paramount concern.

Other varieties of the notion of security in other nations also emerged from the collective experience of economic downfall and ensuing collective solidarity. The term social security originated in the US in the 1930s as a response to economic depression triggered by the Black Friday at the stock exchanges in 1929. The British version of social security and welfare state associated with the name of Beveridge emerged in the 1940s out of the collective experience of the Second World War.

China, by contrast, has been shaped by the experience of mass poverty and government inaction in the 1930s and less by the extinction of the assets of a broad middle class. This helps explain why poverty reduction and returns seem to prevail over the aim of security in current social policy making. However, the PRC social security culture or welfare culture is only in the

making. It is difficult to predict, for example, how a crash in the financial markets that would affect large numbers of pensioners in the year 2030 might impact on the attitudes of the people toward matters of security.

The institution of retirement has recently been questioned. First, retirement under public benefits has been seen as dependence on the state, as loss of autonomy for the elderly. While it is true that living on public pensions makes people dependent on the fluctuations of government decisions on pension levels and finance, cash benefits, unlike personal social services, leave every freedom of action to the person who receives it. Second, most prominently in the US, a statutory age of retirement was seen as a form of age discrimination and as an inroad into the free choice of individuals. This led to legal changes that allow people to work beyond the age of retirement if they so wish. The question then is, if the PRC should do without a compulsory retirement age and introduce a more open entry into retirement right from the start. Kohli (2000) argues that the answer to be given depends on the culture of the country. Based on empirical evidence he defends the continental European tradition of politically defined and negotiated age limits. In the Anglo-Saxon tradition a more liberal, less political concept of transition into old age may appear more adequate.

1. The Generational Contract

The idea of a just reward for a lifetime's achievement points at an underlying individual morality. But there is also a collective morality of public pensions based on solidarity. Any kind of provision for old age rests on some kind of generational contract. This is most visible in the case of public pensions financed on a pay-as-you-go basis. The younger (or middle aged) generation supports the older generation by paying contributions. In turn they are entitled to support from the younger generation when they are old themselves. This is a two-generation contract between the middle aged and the aged, a general pattern of mutual obligation to be continued over the chain of succeeding generations.

One might argue, as the *doyen* of Catholic social science and moral philosophy, Oswald von Nell-Breuning, has done, that it is even a contract between three generations: The elderly are entitled to benefits not (not only) because they paid contributions when they were younger but because they raised their children who in turn are obliged to support their parents in old age. This is to transfer the generational contract from the family to a national insurance scheme. The idea of a three-generation contract highlights the problems underlying the recent fertility decline in Western populations, namely the failure of new generations to raise children. In this way the basis for the generational contract is eroded.

Contract in this context means a written or more often an informal social agreement based on custom, felt obligation, and cultural traditions. All arrangements for old age assume some generational contract and therefore are vulnerable to those changes in fertility and mortality that undermine the premises on which generational contracts are based. However, the existence of a generational contract can be less visible and less explicit in some forms of provision. In the family the generational contract is most tangible. In the PRC as in many other countries, there is a tradition of a moral obligation to support the elderly that is also enforced by law. In case of conflict, courts put down the terms of this contract explicitly. In Europe well into the 20th century the generational contract in rural families took on a specific written form, in German called the *Altenteil* (elderly's share). When a farmer reached a certain age he signed a contract with his son to hand over the farm. This contract included a right to housing, to food and, in case of illness and other contingencies, to support and care by the younger generation. Economic concern for the farm was combined with social care.

Under national social insurance schemes the generational contract becomes more anonymous and large-scale. It is not a face-to-face interaction between persons as in the family, but is operated by an impersonal bureaucracy that redistributes money between age groups. People become dependent over large distances. If such a scheme were to be introduced in the PRC, the middle aged in Yunnan would unknowingly contribute to the welfare of the pensioners in Shandong. The moral basis has shifted: The personal feeling of obligation is replaced by trust in the operation of the system, i.e., trust in its reliability, in the absence of misuse and corruption, in fairness of procedures, and in the security of the central government that guarantees the scheme. In a huge country like the PRC such a system might be difficult to set up at the national level.

Funded pension schemes or commercial insurance seem to operate without a moral basis, purely on individual self-interest, based on individual accounts. But even here there is an implicit contract between generations, which is even more anonymous and less visible than in the case of pay-as-you-go schemes. Some economists like Mackenroth or Gillion (2000) have argued that participation in any (public or private) scheme for old age implies a claim by the participant to a share in the future gross domestic product (GDP). Households can save but groups and societies cannot. For example, pension funds must sell shares to pay out pensions to those who paid into the fund years ago. These shares will mainly have to be bought by the middle aged of that time. This means that the social product has to be shared between the middle aged and the aged, mediated through financial markets. When in the year 2030 there will be many old people and few middle aged, large sums of money will have to be transferred to the aged, much more than today. This redistribution rests on hidden moral assumptions that will have to be debated, such as who loses and who wins, who cares for the losers and how. Thus also private and commercial schemes may give rise to social conflict.

C. Objectives and Models

We argued that thinking about pension schemes is not only a matter of looking at best solutions but also at making value decisions and choices. Several objectives and normative models of pension policy have to be considered and weighed against each other. They may clash with one another but combinations and compromises will have to be found.

1. Objectives

The four main objectives of pension policy are

- poverty reduction and equality,
- security,
- high coverage, and
- returns.

Poverty reduction has emerged as the overarching goal of international development organizations. As regards social security the tradition of poverty reduction and (to that extent) equality as prime aim is associated with the name of William Beveridge. Beveridge, whose social security report of 1942 led to the British postwar welfare state, stands for the tradition of (low) flat-rate benefits in old age. The other big tradition in Europe is termed after the German Chancellor Bismarck who founded the principle of pensions graded by previous earnings, which

implies that security of incomes rather than poverty reduction is the prime aim (see below). The current reforms of old-age pension in Europe can still be traced to these two traditions (Hinrichs 2000). Another version of poverty-oriented pension policy can be found in the US where benefits are earnings-related in a way that low-income contributors get out more.

For the PRC the aim of poverty reduction is paramount. There might be a case for following the Beveridge tradition, especially in rural areas. But since pension policy ought to take a long-term perspective, the emergence of better-off people, of a middle class, must be taken into consideration, and they may take an interest in earnings-related pensions. The current pilot schemes that built on individual accounts allow better-off people to pay more and get a higher pension later.

However, pensions (as other benefits) that are mainly targeted at the poor tend to be very low. As Richard Titmuss, the *doyen* of British social policy once, remarked: Welfare states that target the poor will have poor services (corroborated by a recent empirical comparative study, Korpi/Palme 1998). Indeed almost a quarter of the elderly in Britain have to resort to social assistance to top up their low pension. The main reason for this paradox is that the middle classes have little self-interest in a flat-rate scheme so that they give little political support for its development.

The objective of *security* enshrined in the Bismarck tradition implies earnings-related pensions designed to preserve the life standard attained during working life. Such a system will be much larger, financially and administratively, than flat-rate pensions. It may be combined with the anti-poverty approach by adding a floor, a minimum pension for those who could not pay enough contributions. In the case of Germany poverty in old age could be almost abolished although the scheme has no built-in minimum. This is due to the high level of benefits in a rich country with a generous pension system.

Security is an indispensable component of social security. But only contribution-based or tax-financed systems can guarantee benefit levels (defined benefits). Funded and commercial schemes based on defined contributions cannot normally achieve this objective.

Objectives of social security may include a certain degree of *coverage*. The first two objectives, poverty reduction and security, refer to benefits but leave open the group of people who shall enjoy them. Three main types of coverage can be distinguished.

- Universal schemes extend to the whole population or citizenry.
- Categorical schemes are directed to designated groups, for example in the PRC to urban workers.
- Targeted benefits are also directed to a certain group but this group is also defined not only by reference to general socio-demographic characteristics but also by need. Means-tested social assistance is a targeted scheme.

In the PRC, the Minimum Living Standard System is based only on need, whereas the Five-Guarantees Scheme rests on the Three-No's. Benefit level and coverage can be conflicting aims. In the PRC the question may well be, level or coverage (Cook 2000)? For example, should the level of urban pension benefits be lowered and state subsidies be reduced to provide funds for increasing coverage of pensions in rural areas?

An important issue is whether participation in the scheme shall be voluntary or compulsory. Both strategies have advantages and drawbacks. Compulsory participation raises

the problem of acceptance and may lead to evasion, both on the sides of the individual participant and employers. It may also be seen as an infringement of individual rights. On the other hand, voluntary participation may lead to the exclusion of those who are most in need because they cannot pay contributions. At the same time good risks—the better-off in the case of pensions or those in good health in the case of health insurance—may choose not to join the scheme, thereby leaving behind those who pay less contributions so that the scope for redistribution is curtailed.

High *returns*, though often mentioned, are not an original aim of social security. It may clash with the aim of security. Public pay-as-you-go schemes that have just started to operate normally offer excellent returns and security at the same time, while more mature schemes offer security rather than good returns. Conversely, funded schemes, public or private, that operate on the basis of defined contributions may offer higher returns but less security. When the plan for state subsidized private provisions for old age in Germany was drafted in the year 2000, it turned out that several private providers would not qualify for subsidies because they could not even guarantee that participants make no loss. However, there are ways to weigh the competing aims of security and returns against each other.

2. Normative Models

The objectives of social security leave open by which models they are to be implemented. If we look at security systems as a whole—including their moral foundation, benefits, eligibility, and finance—we can distinguish three major types named by their dominating normative principle:

- achievement-based schemes,
- merit-based schemes and
- needs-based schemes.

The welfare system of one country normally encompasses at least two, sometimes all three of these types. Different types may even be combined within one social security scheme, but normally one of the three normative principles dominates a scheme, at least as perceived by the citizens.

Achievement-based schemes provide benefits that are related to previous earnings, corresponding to contributions paid by the employee and the employer during working life. There may also be some state subsidy but only as a supplement. Such schemes are akin to the objective of security. Their weakness is the linkage between benefits and employment. They tend to disadvantage women because women tend to have fewer years in employment, do more unpaid work without paying contributions and, when they are employed, on average have lower wages than men. Similarly, unemployment and other interruptions of working life diminish both the individual and collective basis of entitlements.

Social insurance schemes are often achievement-based but this is also the case for commercial and private insurance. However, private schemes are achievement-based in two ways: They reflect achievements in working life through the amount people pay into the scheme but they also reflect the achievement of successfully investing the funds. The investment of funds is normally beyond the control of the participants so that bad investment might ruin the outcome of a life's work. In this sense these schemes are less (less reliably) achievement-based than social insurance. Interruptions of employment carriers, by unemployment or in female careers, are equally problematic for private schemes because people cannot pay

contributions or premiums. It may be even more problematic than for social insurance because there is normally no direct subsidy that could make up for these gaps.

Merit-based schemes may also reflect the employment record of a person and be achievement-oriented to that extent but they primarily define eligibility to benefits on the grounds of merit to the country or the nation. Typical groups to whom such merit is attributed include

- cadres,
- civil servants,
- service men,
- victims and veterans of war.

As can be seen from this list, beneficiaries normally have some kind of relation to the state. Merit-based benefits are normally tax financed, not by individual contributions. Benefits tend to be high because of the importance attached to these groups by government. They enjoy privilege and political power. The problem is that this reduces the resources available for the non-privileged. Especially in times of social reform the beneficiaries of merit-based schemes may successfully resist far-reaching changes.

Because of their strong state tradition both the PRC and Germany have substantial merit-oriented schemes. In Germany the civil servants, with their separate and privileged provision schemes, have up to now successfully averted retrenchments imposed on the majority of the population covered by social insurance. In the PRC the merit-based schemes are not normally mentioned in discussions about reform and rectification.

There is another merit that is recognized as a basis of entitlement in the PRC only: To have only one child (or two daughters) or to be a single child. Special allowances are provided for these cases. There have even been separate benefit schemes like special subsidies to commercial insurance. Also at the village level, subsidies to contributions for old-age pensions are sometimes paid to one-child parents and other groups of merit mentioned earlier.

Need-based schemes do not require achievements or special merit but only need of the person in question. They are normally means-tested—or ‘targeted’ as the sometimes euphemistic term goes—and most closely match the objective of poverty reduction. In these systems need is what governments and administrative agencies define (normally fairly narrowly) as need. This type of benefits is tax financed. In the PRC, it is found at the local level in the form of Five Guarantees, Poor Relief, Disaster Relief, and more recently the Minimum Living Standard System. Need orientation basically means social assistance.

Such schemes could provide for old age in three ways.

- The elderly could be covered by general social assistance schemes to which other age groups are also entitled.
- A special means-tested scheme could be created for the elderly, possibly with a slightly higher level of benefits than ordinary social assistance, as in Australia.
- Social assistance, as the last safety net, will always act as a supplement for those elderly with insufficient pensions.

In those countries where this applies to a larger proportion of the elderly, social assistance has in fact turned into a scheme largely (though not exclusively) for the elderly. As mentioned earlier, in Britain almost 25% of the elderly have to resort to social assistance to

top up their pension. In Germany in the 1960s the elderly were the biggest beneficiary group of social assistance. Though need-based systems may, depending on the level of benefits, reduce poverty there remains the problem of the stigma. People may feel ashamed to take it up, and many of those eligible will not take it up at all. A problem of exclusion arises.

The PRC and Germany are two of those few countries where all normative models—achievement, merit, and need as normative principles—play a substantial role and together make up a tripartite system of social welfare (for the PRC see Cook 2000). While in Germany the tripartite structure is explicitly referred to in the public debate as the normative basis of the welfare state, it is hardly mentioned in the PRC debate. It waits to be seen if in the PRC, like in Germany, the merit-based schemes close to the state will be able to retain their privileged position.

With regard to the PRC, it is also worth noting that a developing country like it has developed a substantial achievement-based scheme so early (in urban areas). As discussed earlier, this is related to the specific function of the urban workers in the process of nation building. Therefore, in the case of the PRC, the strong role of the state has not only fostered merit-based schemes but has also enabled an achievement-based sector of the welfare system to emerge.

The third model, need-oriented social assistance, is inferior to the other two as regards benefits and conditions of take-up. But even if its scope can be reduced in the course of economic growth and welfare state expansion, it remains an unavoidable last safety net for atypical cases not covered by the more standardized achievement or merit-based schemes (Marshall 1981). The PRC is also special with regard to need-based systems because, uncommon in developing countries, there is a uniform national framework for those schemes, mainly Five Guarantees, Poor Relief and Disaster Relief, and a modern scheme of social assistance, the Minimum Living Standard System, is being tried.

3. Towards an Integrated Policy—Pension Reform is Welfare State Reform

To sum up: the PRC has a pronounced tripartite structure of public welfare provision that is found in some Western welfare states with a strong state tradition, but which is not common in developing countries. The tripartite structure has three components.

- *Merit-based schemes* cater for state-related employees like cadres and servicemen with fairly generous benefits to secure their active support of government.
- *Achievement-based schemes* are mainly an unusually substantial urban old-age pension scheme that cater for the industrial class base of socialism to secure their loyalty.
- *Need-based schemes* provide for those who have no other private or public income. There is a variegated system of older social assistance-like schemes that operate at the village level within a (rare) unified national framework and a more recent scheme (MLSS).

The system becomes more complex by the division rural-urban in welfare provision, which cuts across the tripartite structure (Table 8).

Table 8: The Structure of the PRC Welfare State—Key Benefit Schemes

Moral Basis	Achievement	Merit	Need
Urban	Industrial workers pensions	Provisions for cadres, civil servants, servicemen/ex-servicemen and veterans	Allowance for laid-off employees, Minimum Living Standard System
Rural	Farmers' pensions (pilot schemes)	Social preference (<i>shehui youfu</i>) payments to ex-servicemen and veterans; preferential subsidies for village cadres for pension entitlements	Five Guarantees, Poor Relief, Disaster Relief; social welfare/ Residential care (<i>shehui fuli</i>); Minimum Living Standard System in some areas

Note: for a more detailed description see Cook (2000: 11, 33-35, tables 1,2).

The highly developed tripartite structure adds up to a welfare state. Although the term welfare state seems to be dreaded by many PRC policymakers and administrators—mainly because they feared the risks of soaring social expenditure and weakening work incentives—there seems to be no reason not to think of the PRC as welfare state. In fact the PRC seems to be on its way toward establishing a welfare state, as can be seen, for example, in the introduction of a Minimum Living Standard System as a kind of modern social assistance and in urban pension reform.

Esping-Andersen (1990) distinguished three types of welfare states or welfare regimes: the liberal regime (including the US), the social democratic regime (including Sweden), and the conservative regime (including France and Germany). The conservative regime bases entitlements on status, not on national citizenship or need as the other two regimes. Different status groups have separate provision system. The PRC is closest to the conservative regime because entitlements differ sharply between urban and rural citizens and between government officials and workers.⁵

In a country with a socialist legacy, a pronounced welfare state structure cannot come as a surprise, although the principles of socialism are not the same as those of the welfare state. Under socialism social welfare provision was conceived to be organized at the level of the work unit and in the living quarter. Welfare states in market societies, by contrast, rely on a social differentiation (separation) of production in the economic market and the supply of welfare services in independent, separate institutions like social insurance agencies or voluntary welfare organizations. The PRC is following this path in current urban pension reforms by largely freeing the operation of the enterprises from the provision of social security benefits.

Still socialism with its strong state tradition must be seen as a source of the unusually pronounced welfare state character of the PRC society. The attitudes of citizens and officials toward this welfare state, however, seems to be paradoxical. The recent rejection of large-scale state bureaucracies and overall state control seems to foster an attitude of going to the other extreme, namely to reject any kind of state intervention, an attitude that sometimes may even go further than US American neo-liberalism.

In setting up rural pensions, it is important to have the whole structure of the welfare state in view. Pension reform is welfare state reform. This not to say that the different social

⁵ For the recent debate on welfare regimes in East Asian countries see, e.g., Kwon (1999: 83). For a seminal analysis of the stratification of social entitlements in the PRC see Bo (1999).

security systems should all be merged into one uniform system for the entire population. Neither does it mean that all single systems ought to be reformed at the same time, which would be an overload for the political system. But an integrated policy would mean to review basic decisions that were made 50 years ago and to revise institutional structures that have grown wild over the past decades. The current reform of the urban pension system is a first step, but the rural system, the merit-based system for public sector officials, and need-based social assistance must be included in an overall reform plan (boxes 1 and 2).

**Box 1: Reform of Old-Age Security is More Than Pension Reform
—Towards an Integrated Policy**

All three components of the welfare state—merit-based schemes, need-based schemes, and achievement-based schemes—have to be included in the reform.

- The elderly are catered to in all of the three system types. State-related employees like cadres and servicemen age just like urban industrial workers and, for example, the Five Guarantees Scheme caters almost exclusively to the elderly.
- The three components are linked, e.g., if people change careers or when insufficient merit or achievement-based benefits lead to entitlement to need-based benefits.
- All three components are affected by the foreseeable ageing of the population.
- All three are or should be related in the design of reform policy: The ageing of the population concerns the country as a whole and the burdens should be carried by all taxpayers and not only by reducing benefits for urban pensioners. Government subsidies should be weighed between the three sectors and not be decided separately.
- Rural and urban pensions are equally linked and should be treated together in policy making. This becomes inevitable with the increasing blurring of the rural-urban distinction due to TVEs and migration. The original PRC social contract about divided rural-urban welfare arrangements needs revision.

Box 2: Policy Guidelines for an Integrated Reform

- The policy design for rural pensions ought to be embedded in an overall policy plan that includes the entire structure of welfare provision.
- Different departments of Government that are responsible for different components of the structure ought to increase cooperation and coordination, e.g., by setting up joint committees. This is currently little developed.
- The inertia of established commitments and the vested interests behind established merit-based entitlements for cadres, servicemen, etc., must be faced in any reform process.
- The value decisions and choices within the overall welfare state structure should be made explicit. The divisions that imply privilege and disprivilege should not be taken for granted.

D. What is Social Insurance?

Social insurance is a key model in social policy. It is especially interesting for the PRC debate because it is primarily financed by individual contributions, not by taxes, and thus relieves Government of the threat of soaring social expenditure. Social insurance can be seen as a kind of collective self-help.

The urban pension scheme in the PRC is an (immature) variety of social insurance, but it has been a matter of controversy if the rural pilot schemes set up by the Ministry of Civil Affairs are a social insurance or not. Even in the Western debate the precise meaning of the term is not settled. In the Beveridge tradition the term has a broader meaning than in the Bismarckian tradition. Sometimes it is used to cover almost any type of public income maintenance other than social assistance. However, to make meaningful distinctions, a stricter definition of social insurance is advisable. Among the three bases of entitlement described in the preceding sections—achievement, merit, and need—social insurance is most closely related to achievement. But there are many varieties of social insurance. The dominating principle of achievement may be supplemented by others.

Like private insurance social insurance is based on the assumption that there is a risk (like old age or ill health), that there is a group of people who might suffer that risk, and that the likelihood of that risk to actually occur can be calculated. The insurance provides a risk compensation between the members of that group.

The key characteristics of social insurance are

- compulsory participation,
- social redistribution,
- nonprofit operation, and
- an independent agency that administers contributory funds and entitlements (unlike merit- or need-based systems that are administered and financed by the Government).

Compulsory participation: Social insurance is mainly financed out of contributions by the participants (and possibly also by employers), so compulsory participation means compulsory payment of contributions. Any compulsion is an infringement of individual rights, so reasons must be given if such a strategy is adopted.

One rationale is the assumption that people tend to be shortsighted and need guidance to their best long-term interest. The second rationale is to create a big enough group of people to serve as a basis for pooling funds for risk compensation. Especially better risks, like healthy people who might not want to join a health insurance, shall be forced to join, or, in the case of old-age pensions, those who pay higher contributions due to higher income should also join. A third rationale is to force poorer people to participate and pay contributions during working life to make sure that they do not fall onto public funds (social assistance) in old age. For private insurance this rationale obviously is irrelevant but it matters for public schemes. A fourth rationale is the low administrative cost as compared with private insurance. When people are compelled to join there is no need for a large number of sales agents who have to go to each village to advertise the scheme.

All these points are relevant to the PRC, especially to rural PRC. Administrative cost for private or commercial insurance in rural areas is so high that they tend to retreat from those areas. With the introduction of the Minimum Living Standard System, which provides benefits when a person's income falls below the poverty line, the threat of uninsured people to fall onto public funds in old age has become very real. As regards guiding people to their best interest and trying to include better risks, local governments in rural areas have up to now relied on a strategy of voluntary participation, though combined with massive campaigns and other measures like letting local cadres take the lead in participating. This strategy seemed to be better suited to secure acceptance among the population.

Redistribution. Any insurance, public or private, implies risk compensation. This involves a massive redistribution among the insured. For example, a person who has paid into health insurance during his whole life without being seriously ill has got little returns from his contributions, which were instead used to finance medical services for less healthy people. Similarly, in private provision for old age, people who die early may lose compared with people who live longer and enjoy their annuity for a longer time. But even the losers get something—security—although in financial terms they may suffer losses.

Normally a distinction is made between risk compensation as just described and social redistribution, which shifts money from higher income to lower income people. Examples of the latter include minimum pensions, modifying earnings-related benefits so as to profit low earners like in the US or, as in the German case, extra benefits for noncontributory years, e.g., for times of higher education or raising children. The normal assumption is that private or commercial insurance is confined to risk compensation without redistribution, while social insurance adds redistribution to risk compensation.

But it is misleading to see redistribution as the typical characteristic of social insurance, for two reasons. First, social insurance is not primarily about vertical redistribution between rich and poor but about horizontal redistribution within the life course of one person. The leading objective is security within the life course, transferring money from one life phase to another, and not equality among the insured. The German political scientist Fritz Scharpf used the expression socialism within one class to highlight the nonegalitarian character of this type of distribution.

Second, as Gert Wagner (1984) has shown, risk compensation and social redistribution overlap and cannot clearly be distinguished. Private insurance also involves redistribution. One example is how men and women are treated. Private insurance defines certain risk groups to which their calculation of the probability of the risk refers. The benefits and premiums of this specific product or tariff group are calculated on this basis. Since women have a higher life expectancy as men they may have to pay a higher premium. Actuarially speaking, they are a higher risk. In social insurance, by contrast, men and women are treated alike. However, a private company may choose to offer a unisex tariff that also treats men and women alike. Strategies of insurance companies and other private providers for old age are not fully determined by actuarial calculations. Companies offer a product in a market, aiming to meet the demand by consumers. If a unisex tariff can be successfully sold it can be provided without problems.

We may conclude that through compulsory participation social insurance is in a position to broaden the pool for risk compensation. We can also say that social insurance makes more explicit choices about redistribution whereas in private insurance such choices are made by the companies and are less visible, as the example of the unisex tariffs shows. Normally they are beyond the scope of government intervention though this need not be the case. The German Government has forced private insurance to offer a unisex tariff for long-term care.

If redistribution in the classical sense—paying benefits that are not related to previous contributions—is not desired politically, it is still possible to adopt a social insurance model. This can be achieved by the model of adequate financing (Schmähl 1987), i.e., financing earnings-related benefits out of contributions while financing elements of social redistribution out of government subsidies. Even though, as described, the dividing line between these two kinds of benefits is blurred, the size of redistributory benefits can be roughly estimated. In the German

system, for example, they amount to about a quarter of the expenditure, and government subsidies roughly correspond to that proportion. Another option is to let third parties pay contribution, for example, the unemployment insurance can pay contributions into the pension scheme for each unemployed person.

Nonprofit operation. Commercial insurance may not only be more expensive because of higher administrative cost but also because they make a profit that, other things being equal, reduces the volume of benefits that can be paid. However, the crucial clause here is "other things being equal." In a well-functioning market with well-managed private companies, we may assume that the profit orientation acts as an incentive to make the administration and investments of funds more efficient and to offer better, more consumer-oriented products. This may include offering a broader choice of products and products suited to changing individual needs. In that case the profit-based operation of a private scheme need not reduce the level of benefits but may even increase the level and quality.

Independent agency. An independent administrative agency secures relative institutional autonomy to social insurance. This characteristic may be less familiar, though it is a major reason for the strength of this particular form of organizing social security. The feature is less pronounced, less visible in the Beveridge tradition. In contrast to both needs-based and merit-based systems, social insurance benefits are not paid out of the general government budget. Based on individual achievement of the participants, contributions are managed in separate funds. Ideally these funds are less susceptible to arbitrary government interventions. They cannot easily be shifted to fill gaps in other areas of government.

Contribution-based entitlements may assume the character of rights. This is most pronounced in countries with a strong social insurance tradition. In Germany, by rule of the supreme constitutional court in 1980, entitlements to old-age pensions have assumed the status of property rights. This fundamentally changes the position of workers in society. While Marx characterizes them as basically property-less, as citizens of the welfare state they may assume the status of owners of property of a different kind. In this way, entitlements to public pensions have a firm base. They are not funded like claims to certain assets in the financial market, but they are funded by legal claims to future shares in the budget of the insurance agency that is an independent public agency under public law.

All in all, to opt for social insurance does not necessarily mean to go for wholesale social redistribution, more government spending, and collectivism. In the beginning of this Chapter, we argued that social policy making is not about choices between pure models. Social insurance itself is a mix of different values and institutions, a hybrid scheme. It is collectivist and state-oriented insofar as participation is compulsory and there may be elements of redistribution from richer to poorer members. But at the same time social insurance is also decidedly individualist because funds mainly derived from individual contributions and benefits are earnings-related, thus mirroring individual achievement in the market. In this way social insurance reinforces individual responsibility and market values. For tax-financed provisions this does not apply.

Conversely, private or commercial insurance—or more generally private providers of security for old age—cannot simply be identified with noncompulsory and nonredistributory provision. In fact there is a range of possibilities. Participation in private schemes can be made mandatory, as in Chile; it may include some redistribution that may even be prescribed by government like the example of unisex tariff, and a broad range of government regulations are normally in place to frame the operation of the scheme. In any case the state has to act as a provider of last resort, namely to provide social assistance if the insurance provider insufficient

benefits. Commercial insurance, if looked at closely, basically is a public-private partnership, especially in the PRC where commercial insurances in many respects have a strong state character.

E. Summary: Models of Old-Age Security

In this Chapter we have laid out the normative choices available for pension reform and the related institutional designs. We have also shown that the PRC social security system already encompasses a broad range of schemes. Before the current arrangements for old-age provision in the PRC are put to an empirical test and issues of reform are analyzed in the next Chapter, this section summarizes the findings (in Table 9).

Table 9: Models of Old-Age Security in China – Rationales and Capacities

Models	Traditional		Public			Commercial / funded commercial or public funded schemes
	Land	Family	Provisions for Public Sector Employees (excluding SOE)	Social Assistance	Social Insurance (PAYG)	
<i>Moral Base</i>	need	felt obligation	merit	need	achievement, self-reliance	achievement, self-reliance
<i>Real Base</i>	soil, agricultural market	children	taxes	taxes	contributions from younger generation: generational contract	capital in financial markets, contract with pension fund
<i>Benefit Standard</i>	none	custom /malleable	high, politically defined		security (earnings-related defined benefits)	none (returns from defined contributions)
<i>Rights Base</i>	strong (long-term holding)	weak	weak	weak	strong (public law)	medium (private contract)
<i>Agency</i>	land and agricultural authorities	(State Family Planning Commission)	central government	local government	semi-autonomous body	commercial providers, financial markets
<i>Risks</i>						
<i>Ageing</i>	medium	high	high	high	medium (contested)	low (contested)
<i>Fiscal Overload</i>	low	low	high	low/rising	low/medium (subsidies)	low
<i>Unemployment</i>	low	high	low	rising	high	high

The overarching finding is that choices are not that simple as often assumed in the PRC debate, especially by those people who are critical of rural pensions or even social security as such. The great alternatives—family support and land versus pensions, public versus

commercial, self-reliance versus dependency on state provisions—are misleading. Rather there is and ought to be welfare mix, a mix of different models and values.

The elements of the mix are linked. Especially, the Government has a hand in virtually all forms of provision by providing a regulatory and sometimes also financial framework. Family support is legally enforced and the use of land as social security for farmers is based on a tight system of land use peculiar to the PRC. Commercial provision, too, is not just commercial but depends on public support in many ways. The lesson to draw here is to go beyond the public versus private debate and to forge creative links between the two by public-private partnerships.

Even within the public domain, there is a mix: Old-age pensions for workers and farmers; merit-based schemes for civil servants, cadres, and servicemen; and various forms of need-based social assistance—they all cater to the elderly. The lesson for successful reform policy, if you want to reform pensions look beyond pensions.

Table 9 shows that all models of welfare have their specific strengths and weaknesses. There is not one model that solves all problems. Family support and land generally bear low risks but tend to have a weaker performance. Above all they have no or malleable standards of provisions. That is why insufficient provisions and failure are not normally measured and are less visible. Politically this may be welcome when reference to family and land is used to argue that pensions are not needed.

Public provisions, especially social insurance, are better than their reputation. They are based on the idea of achievement and self-reliance just as commercial provisions and equally foster market values. Social insurance forces people to take a long view of their lives and to rely on themselves for the future. Social insurance also serves the economy: Enterprises use it to externalize social cost, and the introduction of a legal age threshold for retirement is a major lever to regulate the labor market.

Entitlements to benefits under a pay-as-you-go system are not less real than entitlements based on capital funds. In Germany these entitlements have the status of property rights and like these can be claimed in court. The generational contract is legally enforced.

Moreover, one rationale of social insurance is to keep the burden of tax-financed social assistance low, thereby reducing the number of people subjected to stigma and dependency on the state. One may predict that expenditure for social assistance and for provisions for cadres, civil servants, and servicemen will become an issue of debate in the near future, whereas political attention up to now has mainly focused on pensions.

Table 9 also reveals that commercial provisions and funded public schemes have certain problems rarely mentioned in the PRC debate. They normally have to do without benefit standards because benefits depend on returns in financial markets and on success of the institutional investor to which a person has entrusted the provision for his or her old age. People hope for high returns but these are subject to market fluctuations. People unable to pay contributions due to low income or unemployment are a problem for funded schemes just as for pay-as-you-go schemes.

To what extent commercial schemes can cope better with the foreseeable ageing of the population is contested among scholars and international organizations. A key use of commercial schemes for politicians, however, is the depoliticization of old-age provisions that it implies (just like land and family support). Compared with public schemes there are no

standards, fewer criteria, a weaker rights character, and generally less public attention to its performance. Any provision for old age implies some kind of contract between generations but pay-as-you-go based social insurance makes this contract more explicit. It lays open the need for redistributing an increasing share of national income to the elderly in an era of ageing populations.

Chapter 4. LEARNING FROM OTHER COUNTRIES?

When Western societies began setting up modern social security systems in the late 19th and 20th centuries there were few models that they could turn to. Once the first social insurance scheme was established (in Imperial Germany in 1891), policymakers took an interest in the schemes of other countries. British administrators around 1900, for example, had a close look at the Bismarckian model. Today the situation is different. Developing and transitional countries can draw on the experience of a wide range of developed Western welfare states. Diffusion of knowledge and exchange of experts through international organizations and bilateral contacts with foreign governments has become common. During the current phase of restructuring the European social model, watching and debating the experience of reform pioneers plays an important role in Europe, too.

Learning may mean to taking over elements of a foreign system. Japan, for example, has adopted much of German social law, most recently key elements of the newly created long-term care insurance. Learning may also mean receiving stimulation and developing other ideas in one's own national context. Third, there is also negative learning, in taking a foreign experience as an example of what is not wanted. In Asia, especially in Malaysia and Singapore and partially also in the PRC, such attitude can be found with regard to the Western welfare state. Some political leaders see it as a failure not to be emulated. They want to stay away from this principle of social organization deemed to be economically dangerous by pushing up fiscal burdens and eroding work incentives. In this view a commitment to building a welfare state is to unleash dynamics of unlimited growth that cannot be checked. For the PRC, the question is if the welfare state could become the third great import from Western societies after Marxian socialism and the market economy.

There are three key questions about learning in the field of rural pensions that were also put by policymakers we interviewed.

- Is it too early to introduce pensions in rural areas? Did Western countries not adopt provisions for farmers at a later historical stage?
- Is it too risky? What long-term risks do we run when establishing a formal commitment to providing for the rural elderly? Are we facing soaring expenditure especially in this subsidy-prone clientele? Are we eroding the traditional work discipline of farmers? Are we unleashing a growth in bureaucracies, clientele, and benefits?
- Which institutional design would suit the needs and conditions of this specific group? Should farmers be covered by a separate system or rather join other systems? How should pensions be financed considering that farmers are not employed and what benefits are conceivable in the face of low resources in this group?

Two groups of countries may figure as models: Developing and transitional countries on the one hand and developed Western welfare states on the other. Attempts at covering the rural population in developing countries have failed almost everywhere (Jütting 1999; Gillion et al. 2000). However, the issue is on the agenda. Governments in developing countries are beginning to take initiatives to tackle the unequal treatment of farmers and nonfarmers in social security. Like the PRC, they feel the need that something has to be done. However, learning from these countries is limited, simply because such examples hardly exist. A few can be found among transitional countries.

For the PRC, the transitional countries of East Europe are of particular interest because they are also undergoing a transformation process from state socialism to a market-oriented economy. Furthermore, Chile may be worth looking at because it has received much attention in the general pension debate in the PRC (Box).

Box 3: Chile—A Model for Rural PRC?

Chile pioneered mandatory private insurance for the employed population in 1981 and became a focal point of reference in the global move toward pension reform in the 1990s. The Chilean system is riddled with problems. Rather than reiterating the general debate about the Chilean model, the question here is if it provides a viable model for rural PRC.

The Chilean pension system does not provide a model for rural PRC because one of its key problems is coverage. Only persons in waged formal employment are covered (plus voluntary low participation by self-employed), thereby excluding almost half of the economically active population. Furthermore, less than half of the insured waged persons are active contributors, the others pay no or no regular contributions (Schulz-Weidner 1999; Gillion et al. 2000). Due to lack of formal employment and poverty, farmers are not a suitable clientele for this type of pension system.

When looking at Western precedents we obviously ought to focus on earlier stages in history because today agriculture in these countries is very different from that in the PRC. Keeping this in mind, the PRC can learn rather more from earlier Western examples than from current developing and transitional countries for three reasons.

- Some of the European countries, especially those at the Mediterranean rim like Portugal, were extremely poor and agrarian until recently, in some areas resembling developing countries.
- The European rural economies faced and still face similar structural problems as the PRC: The change of agriculture, its shrinking, and its transformation through technology and commercialization; the nonwaged status of many farmers since, unlike large-scale industrial agriculture found in the US, family farming prevails in most European areas; and low incomes among the farming population: even in better-off countries farmers tend to be relatively poor, unable to join general pension schemes under normal circumstances.
- Since Western countries have developed complex institutional arrangements with a long reform history, the PRC can learn about the specific institutional design of pensions for farmers. The need in pension policy to plan for the future urges thinking about institutional details well in advance.

This Chapter proceeds as follows: First we analyze the specific problems of setting up a social security system in developing countries (section A), especially in rural areas (section B). This shows that problems the PRC shares with other developing countries and where it differs. The analysis of developing countries also helps explain why they have not normally set up formal old-age security systems. We then ask what the PRC can learn from other developing and transitional countries (section C) and from Western countries (section D).

A. Problems of Social Security in Developing Countries—is the PRC Different?

There are specific conditions in developing countries that have to be taken into account when designing welfare systems:

- the scarcity of resources,
- the employment structure,
- the limited administrative control capacity, and
- the low development of the legal system.

The first limiting condition is the *scarcity of resources*. Incomes tend to be low and fluctuating, there is much poverty, and urgent needs prevail so that even when some money is left that could be spent for social contingencies it may be used to satisfy more pressing needs of the day. Also state revenue tends to be limited so that there is little money to tax-finance welfare benefits and to set up a sound administrative structure. But even in poor countries government spending is a matter of setting priorities. Political factors account for how money is spent. Privileged groups, mostly people close to government, are more likely to succeed in getting state support. Besides, governments, even if they are committed to the welfare of the less privileged citizens, may prefer to invest more money in economic and structural development of poor areas than in social security benefits aimed at individuals.

The second major hindrance is the *employment structure*. Contributions and taxes are difficult to collect and benefits difficult to pay out when large sections of the workforce are not in waged employment but belong to the informal sector, are self-employed, agricultural smallholders, or even unemployed. Widespread seasonal work and occasional employment add to these problems.

The third problem is the limited *administrative control capacity* in most developing countries. The efficiency and the effectiveness of public administration, as regards fiscal policy, the implementation of social policy and related capacities, tend to be low. Lack of training and qualified social professionals and of information systems is common, and corruption, protectionism and pressure by interest groups prevail and lead to high cost. The political environment is not conducive to sustaining social security systems. Canvassing new schemes to secure acceptance may be insufficient. Politics may change so rapidly that trust in institutions cannot develop. Different levels of government may be insufficiently coordinated so that central policy decisions cannot be translated into local service delivery.

However, private or commercial institutions in such countries tend to be equally weak and unstable, such as financial markets and corporate investors. Countries face the dilemma that, lacking the capacity to run a public welfare scheme orderly, they will normally also have a low capacity to regulate and control private provisions.

The fourth weak point in developing countries often is the *legal system*. For social legislation to become effective several conditions have to be met: People have to know about the law and their rights; they must be able and willing to claim their rights; and governments and public agencies must be in a position to enforce the law (Kaufmann 1982). Tax (and contribution) evasion, both by employers and by participants, tends to be a major problem of insurance schemes. Again, this problem also arises for private providers as can be seen in the case of Chile where the private providers fail to enforce regular payment of contributions. In view of not

detering customers, they do not press too hard if contributors do not pay (Schulz-Weidner 1999).

Furthermore, legal institutions must be set up, surrounded by a gradually evolving culture of law. Statutes, i.e., legislation passed by parliaments instead of mere decrees, courts, lawyers, and legal advice centers are key elements of a modern legal system. On the demand side, a certain level of education among the population is acquired. Access to legal institutions can be facilitated by allowances for legal action by poorer citizens (legal aid) and by a sufficient number of lawyers and legal advice centers in the vicinity of every citizen.

In addition to these four critical points, there are specific problems in rural areas that make up the biggest sector of the economy of developing countries. These rural problems will be specified in the next section. All in all these problems make it most difficult to extend *coverage* of social security systems. *It is now generally accepted that the approach of enlarging state-based social security systems in developing countries in order to achieve universal coverage has failed.* (Jütting 1999). Available statistical figures indicate that, while 80% or more of the workforce is covered by social security schemes in developed countries, the proportion in many countries of Asia and Africa remains below 10% (Beattie 2000). All over the world maybe more than 2 billion people are not covered by any type of social security, neither by insurance nor by social assistance (van Ginneken 1999). It is mainly the rural population, workers in the informal sector—both rural and urban—the self-employed, and the poor of any kind who are most likely to be excluded from social security coverage.

In many ways the PRC shares the general problems of developing countries though in important respects conditions are rather favorable.

As regards scarcity of resources, the PRC has experienced a tremendous rise in incomes over the last 20 years. The Government may soon have at its disposal a substantial amount of resources if it pursues the strategy of selling state assets from the SOEs. The allocation of available resources, however, is subject to political priorities. Urban workers and subsidies to their pension scheme, which is burdened with a huge implicit pension debt, seem to have priority. A transformation of local fees into central government taxes that is currently considered will also change the way resources can be disposed of.

The problems of the employment structure are similar to those of other developing countries. But the proportion of the agricultural workforce, despite restrictions on migrating to cities, peculiar to the PRC, is rapidly declining. Moreover, the informal sector seems to be comparatively little developed.

Administrative and legal hindrances are also shared with other developing countries although since the 1990s institution building in many fields like the legal system (Liu 1999), financial institutions and administration, has been promoted with priority. There is a dilemma peculiar to countries with a state socialist legacy. Large-scale bureaucracies are being scaled down whereas at the same time new and reformed institutions have to be set up. The so-called socialization of social security, i.e., transferring the administration of social security from the SOEs to separate public bodies and government, is a case in point. While the bureaucratic legacy is a problem, the administrative experience and qualification of the staff may also be a resource that the PRC could draw on in the future.

All these factors might explain why coverage of social insurance in the PRC is fairly high as compared with other developing countries. Pilot schemes for pension insurance in rural

areas are not common at all in other countries and the early broad coverage of urban workers is also exceptional. Structural changes like migration and the growth in TVE, however, put the question of coverage on the agenda again.

B. Problems of Social Security in Rural Developing Areas—is Rural PRC Different?

The general problems of developing countries are exacerbated in rural areas. In some respects, though, the rural organization of living may have advantages. Family support may be more engrained in local custom than in urban areas. But this need not be the case, especially among ethnic minorities. The Miao people we visited in Yunnan have a tradition of self-reliance even by the elderly who are not normally supported by their children (see Chapter 6.A). The key asset of rural areas is land, which acts as a base for subsistence. During the Second World War in Europe and its immediate aftermath, the rural population had the advantage over urban citizens of having food. But land may fail as a last resort when natural disasters strike or when mistaken economic policies reduce agricultural output dramatically or both, as experienced in the PRC's recent history.

Five structural problems are typical of rural areas:

- agricultural production and its pitfalls,
- high cost of transport and communication (transaction cost),
- low legal knowledge among farmers and little legal infrastructure,
- low monetarization of the rural economy, and
- rapid structural change.

First, the problems of low-scale and little commercialized *agricultural production* are common to developing countries. Incomes tend to be discontinuous, following the seasons, and under circumstances of natural disasters. Natural disasters like flood, drought, earthquake, and bad harvests constitute "covariate (collective) risks" (Jütting 1999). While risks like sickness or old age occur individually and relatively independently, natural disasters strike many or all inhabitants of a village or an area at the same time. Need for help jumps up massively while local helpers and mutual assistance capacities are also hit and cannot offer aid. This is a problem for locally based security schemes.

Private insurers, in principle, are able to insure against natural disasters although this can only be done on a larger scale by involving reinsurance companies. However, in recent years disasters have taken on such a scale that the insurance industry is seriously concerned and is forced to change its strategy. Under public schemes wider pooling of funds is needed to deal with covariate risks.

Second, high *transaction cost* emerge from difficulties of transport and communications. Farmers in villages live less concentrated. Especially in remote and mountainous areas, transport and communications is difficult. This raises the problem for delivering social services, for collecting taxes and contributions and for paying out benefits. For commercial providers these conditions are no less critical. Life insurance companies face high transaction costs for relatively small contracts (Jütting 1999), making rural areas unattractive to them.

Third, the undeveloped status of the *legal system* is exacerbated in rural areas. Farmers are on average less educated than urban citizens, promoting of knowledge is less easy in

remote areas, and access to legal advice centers and to consumer protection is also more difficult.

The fourth factor is the *low monetarization* of the rural economy. This limits the use of cash benefits like pensions. Money is only one component of the rural exchange of resources. Few things may be bought in shops that can be several kilometres away in nearby towns. The main components of the rural welfare mix are

- subsistence from land,
- money income from agricultural sales, part-time employment in local businesses or small-scale self-employment;
- support by family and kin;
- local collective self-help such as mutual aid, cooperatives, and associations that often provide benefits in kind, like helping on a sick person's land or repairing the house of old incapacitated people; and
- nonprofit organizations such as local or national trade unions and women's associations, charities and national or foreign nongovernmental organizations. The latter are particularly active in rural areas because the fight against poverty that is widespread in rural areas is their key concern.

The low degree of monetarization makes it more difficult to assess the tax and contribution base among rural citizens. To base insurance contributions only on money income will not be adequate. Decisions are needed in which ways assets, subsistence production, turnover from agricultural sales, money income from part-time employment in business, and income in kind are to be taken into account.

Fifth, the *rapid structural transformation* of the rural economy does not lend itself easily to institution building in social security. With increasing urbanization and industrialization, the primary, agricultural sector of the economy recedes rapidly. In such a "dying" rural population, a pay-as-you-go system of financing social security meets with several problems. A decreasing number of contribution payers would soon be left with a much higher number of pensioners. The very category "rural" is changing its character. Incomes from other sources than agriculture, local industry, and migration to towns and cities constantly change the potential clientele of "rural" insurance schemes. Social security schemes targeted at fixed social categories like farmers or defined by area like rural are difficult to operate. Problems include transferring membership between different security systems and dealing with people not covered by any of them.

All of these problems apply to the PRC. Natural disasters affect large sections of the population time and again, and the number of people receiving disaster relief well exceeds a quarter of a billion. The growth of TVEs, however, has provided an outlet and compensation for the limitations and instabilities of agricultural production. Regarding the rural welfare mix, the role of land is even more pronounced than in other developing countries due to the PRC philosophy of land and the legal regulation of land use.

As regards collective self-help at the local level, semi-government by villages committees in administrative and natural villages is the PRC way of formally organized and nationally standardized mutual aid. Other collective schemes include "hand-in-hand" partnerships of government, enterprises, and well-off citizens in helping the poor (sponsored by MOCA) and cooperative forms of social security promoted by the MOLSS and the All China

Trade Unions to supplement the state schemes. Finally, the problem of transaction cost is paramount in the PRC (Box 4).

Box 4: Problems of Territory in Rural PRC

The PRC is a mountainous and hilly country, with mountains accounting for 33% of total land area and high planes for a further 26%, mostly rural. This poses considerable problems of transport and communications. The delivery of social services, especially those relying on face-to-face interaction between clients and social professions, is difficult. But also for cash benefits like old-age pensions, specific problems arise especially with regard to

- the collecting of contributions;
- bookkeeping and comparing insurance records held by participants with administrative records kept at the town or county level;
- delivering benefits if beneficiaries have no bank account or if a bank can only be reached by walking or riding to the next town;
- accessing space-bound collateral services like legal advice centers or consumer protection is equally impaired.
- commercial providers are also affected—Due to high transaction costs for small-scale contracts they tend to retreat from rural areas.

C. Learning from Developing and Transitional Countries?

Due to the difficulty of imposing formal pension schemes in the rural sector, many developing countries have launched self-financed schemes thought to better meet local needs. In some areas local associations or NGOs promote such schemes, which fulfil demands for flexibility and decentralization highly appraised by scholars and developmental planners (Gsaenger 1994, Lachenmann 1994, van Ginneken 1999). In some countries, e.g. Columbia, Philippines, and Tanzania, self-help schemes were established to provide mutual aid in restricted regions or for specific occupations (Gillion et al. 2000). These schemes usually provide certain assistance to their members, mostly in the form of lump-sum payments. In India such schemes can also be found. The local character leads to certain functional limits.

A few countries, however, attempted to include the rural population or part thereof in public schemes. First, some countries tried to include them in the general pension scheme. This was undertaken in Turkey where the principal social security scheme is open to seasonal agricultural workers on a voluntary basis, though on a very low level. Self-employed farmers are members of the pension scheme for self-employed people (Gillion et al. 2000).

The Republic of Korea installed a National Pension Scheme in 1988, with compulsory participation for all private sector employees working for employers with 10 or more employees. The scheme has been extended to mandatory participation of the rural self-employed, farmers, and fishermen since 1995 (Kwon 2001, Son 1996, Gillion et al. 2000). The Korean system may be unique in including the farming population in a defined-benefit scheme under the normal rules for contributions and benefits. However, subsidies are provided, not for benefits but for contributions, making up two thirds of the normal contribution rate of 9%. The scheme is further interesting because the subsidy is conceived as temporary, to be phased out by 2006. This might have helped provide for an almost equal inclusion of farmers.

Second, apparently only Poland—apart from the PRC pilot schemes—has attempted to establish a pension scheme for farmers separate from that for employees. There is a link to the general pension scheme but benefit and contribution formulas vary greatly. The contribution amount for farmers is set quarterly at 30% of the general base or minimum pension of employees (Gillion et al. 2000, Götting 1998).

Third, some countries, such as Romania, offer pension schemes with voluntary participation to the agricultural population (Gillion et al. 2000). These voluntary schemes often lack incentives to attract all farmers, partly because they may prefer to spend their income on other items. The effect of social protection under such schemes therefore tends to be limited.

Fourth, social assistance may be used to cater to the elderly. In developing countries, however, social assistance as a formal scheme is rare. In Eastern Europe, social assistance has acquired more importance. Under quasiuniversal social assistance schemes, the elderly may be included automatically. By contrast, categorical social assistance scheme target specific groups. The national social assistance program announced by the Indian Government in 1995, for instance, addresses the elderly as one of three categorical groups provided for. People older than 65 years, with low incomes, and generally without relatives receive a flatrate pension-like benefit (Gillion et al. 2000).

With the experimental introduction of the Minimum Living Standard System (MLSS) also in rural areas, the PRC became a pioneer of modernizing social assistance. This includes coverage of aged people. Varieties of social assistance are a choice in providing for old age not normally mentioned in the PRC debate. Social assistance differs substantially from pensions because it relies on taxes, not on individual contributions, and is thus prone to create dependence and stigma, not to mention the financial burden for local and possibly central governments (Chapter 3).

All in all regarding proper pension schemes for farmers, few lessons can be drawn from the experience of other developing countries because such experience hardly exists.

D. Learning from Western Welfare States?

The traditional forms of rural provision for old age based on agriculture and family support are no longer sufficient today because of the rapid structural change of agriculture, the difficult economic situation in farming, the changes in family structure as well as changing and novel needs. (Winkler 1992). This statement, referring to the situation in Europe in the early 1990s, sounds familiar. All aspects mentioned equally apply to the current situation in the PRC. Agriculture and rural areas are difficult field of policy in most countries. European evidence suggests that agriculture particularly may become a troublemaker for the PRC for many years to come.

Although it is a very small sector of the economy in present-day Europe, agriculture keeps politicians busy. In particular, it haunts policymakers and administrators of the European Union (EU) in Brussels. As in the PRC agriculture is not a normal sector of the economy like other branches of industry and service that may be left to market forces. Massive subsidies of various kinds allocated to farmers are the single biggest item in the EU budget and a constant source of conflict. With the agrarian East European countries entering the EU, this problem will

be aggravated. Farmers are a strong lobby. In Europe, they have become a "welfare class" whose economic and social position is largely determined and sustained by governments (Rieger 1995). This does not primarily refer to social security provisions but to subsidies and regulation of prices and products; but this, too, is a kind of social policy for farmers and an expensive one for that matter. High national subsidies to social security for farmers add to the bill.

A lot can be learnt from Western countries about the institutional design of rural social security schemes and about the problems that may unfold over a longer time with the maturation of schemes, that is about the question of sustainability.

- Should pensions for farmers be set up at all? Does foreign experience suggest that it might be too early and too risky for the PRC to do so?
- How are farmers located in the general scheme of old-age security: is there a separate scheme or in what ways can they be integrated in more comprehensive schemes?
- What questions of equity arise?
- How are pensions financed? This includes the question of subsidies by government, since farmers in the PRC and elsewhere tend to be less well-off, and the question on what basis to calculate contributions by farmers.
- What supporting services beyond cash benefits are provided?
- What economic effects on the development of agriculture do pension schemes have?

Problems of administration due to remote and less accessible territory and low administrative capacity have figured less in the European experience. Academic research on rural pensions in Europe is very scarce. Like in the PRC there seems to be little interest in the social welfare of farmers.

1. Pensions for Rural PRC—Too Early, Too Risky?

As regards the first and most basic question if old-age pensions for farmers should be set up at all, the message is, No, it is not too early to set up rural pensions in the PRC because several European countries started at a similar or even far lower level of economic development (Table 10). Further, such undertaking is risky, but all European countries took the risk because the process of modernization produced a need for pensions in every country. From this experience it is not likely that the PRC will be able to avoid that risk for a longer time.

Too early? Against the background of European experience, it is not too early to set up pensions for farmers in the PRC (Table 10). Five countries introduced such pensions at a similar or even far lower level of economic development—with the same or even higher proportion of agriculture and with a lower national GDP—as present-day PRC: Denmark, Greece, Portugal, Spain, and Sweden. Among these, Greece was the latest (1961). The Danes came first (1891).

Together with Germany, which introduced old-age insurance (for industrial workers) in the same year, the Danish system was (generally, not only for farmers) the first old-age security systems in any country. Modern social policy began with farmers!

The Danish scheme was (and still is) universal, that is, it covered the entire population. But it did not cover the farmers by chance. Since farmers were almost half of the workforce this could hardly have been the case. In fact, Peter Baldwin in his major study *The Social Bases of Solidarity* (1990)

showed, that the powerful agrarian bourgeoisie pushed for a universal scheme because a categorical scheme (confined to certain groups and based on individual contributions) would have privileged the urban working class. In Sweden the political situation was similar. It was not, as normally assumed, the workers movement and social democracy but the landed elite who founded the Scandinavian welfare state model.

Although there is no agrarian bourgeoisie in the PRC, the message is: It is not the level of economic development that matters but politics. If the political leaders decide to install pensions for farmers they can do it, even at a very low economic level. They may choose not to do it but, as European experience shows, they cannot excuse themselves by saying that the time is not ripe. It is also a matter of politics from below. Unlike the landed classes in Scandinavia, the PRC farmers have no voice in politics, no lobby. They are not organized. Being split into millions of tiny household units and living scattered in a vast countryside, it is difficult for them to form interest groups.

The urban workers, by contrast, always had a strong lobby. It was the interest of government to privilege them. Therefore, the urban workers enjoyed a pension scheme that was and still is much too early, if judged by the level of the PRC's industrial achievement. Contributions to the scheme are much higher than in the German scheme (25% or more as compared with 20% of wages) although Germany is economically far more advanced and runs one of the largest pension schemes in the world.

However, most bigger countries in West Central Europe introduced old-age provisions for farmers only after the Second World War when agriculture already shrank and their general economic level was fairly high. But this is not a model for the PRC because modernization in present-day PRC is unbalanced. The urban sector, industry, and technology are very advanced, while the farming sector lags behind. This sets standards for the aspiration of people in the whole country. The idea of economic progress, new consumption patterns, and new lifestyles are spreading nationwide through the media and through migration. How shall farmers produce for the 21st century when living under conditions of the early 20th century central Europe as regards social security?

Table 10: The Timing of Pension Legislation for Farmers in Europe

Country	Year of First Scheme	Level of Economic Development in That Year			Type of Scheme/ Coverage
		Agricultural Workforce ^a (% of total workforce)	Agricultural Output (% of GNP)	Per capita GDP (Gheary-Khamis \$) ^b	
Denmark	1891	44.9	37.0	2,458	Universal
Sweden	1913	46.2	23.0	3,096	Universal
Portugal	1919	52.7		1,445	Separate (smallholders) ^c
	1977	32.9	11.9	7,498	Insurance for self-employed (big farmers) ^c
United Kingdom	1946	5.1	7.0	6,440	Insurance for employed/self- employed
Spain	1947	48.8	41.0	2,270	Separate (small holders)
	1975	21.9	9.3	9,151	Insurance for self- employed (big farmers)
France	1952	27.0	13.0	5,606	Separate
Luxembourg	1956				Separate
Germany	1957	13.4	7.0	7,154	Separate
Netherlands	1957	10.7	11.0	7,317	Universal
Italy	1957	29.0	17.0	5,008	Separate (smallholders)
	1990	9.0	3.1	15,951	Separate within general system (big farmers)
Greece	1961	55.3	23.0	3,457	Separate
Belgium	1967	5.5	5.0	8,882	Insurance for self- employed
Ireland	1988	15.4	10.3	9,580	Insurance for employed / self- employed
PRC	1999	47.5	17.7^d	3,098	

GDP = gross domestic product, GNP = gross national product, PRC = People's Republic of China.

^a Agriculture includes forestry and fishing. GNP for Spain (1947) refers to 1951. The share of the agricultural workforce could not always be matched with the year of legislation due to lack of data. The figures given refer to Denmark 1890, France 1954, Germany 1961, Italy 1961, Netherlands 1960, Sweden 1910, Portugal averages 1911/1930, Spain 1950, United Kingdom 1951.

^b Internationally and historically comparable measurements of the social product per capita in international Dollars.

The figures given refer to the PRC 1992, Portugal averaged 1913/1929, Spain 1951.

^c Integrated into general scheme in 1984–1987.

^d GDP, primary sector.

Source: Compiled from Winkler 1992, Mitchell, B.R. 1981, Statistics Directorate (Organisation for Economic Cooperation and development) 1960–1993, National Bureau of Statistics 1999, Maddison 1995.

Too risky? The fear of soaring expenditures is justified. Winkler (1992) summarizes the fiscal situation of farmers' pensions in European countries as follows: *No rural social security agency can cover expenses for old-age pensions for farmers and their relatives through contributions. They all need to rely on government subsidies and other methods of finance.* In Germany, for example, subsidies currently amount to 70% of expenditure, and they make up two thirds of the entire budget of the Ministry of Agriculture (1999/2000). Due to the decrease in the number of farmers, however, spending is limited as compared with the other items of the social budget. Agricultural social security can never be self-sustainable: The rural population is shrinking and ageing, leaving behind more elderly people with fewer young people who could contribute to a pay-as-you-go scheme. Funded schemes, public or private, are also difficult to establish since for the older farmworkers it is too late to build up sufficient capital stock whereas the younger are likely to leave and participate in other pension schemes.

Moreover, like most other fields of the welfare state, coverage and benefits of rural pensions tend to expand. In many European countries coverage was intended from smallholders to big farmers, to employed agricultural laborers, and to wives of farmers. Provisions were extended to include survivors' benefits for widows and orphans, accident insurance, health insurance, and provisions in kind.

The overall message, however, is that despite these problems all European countries eventually established old-age security for farmers, either separate or by inclusion in general schemes. The expansion of the schemes reflects needs that arise in the course of modernization in any country. This is likely to be the PRC's near future, too. China should prepare for it now.

Table 10 also shows a variety of forms of inclusion. There is a range of choices on how to include farmers in old-age security.

- Some countries, especially in West Central Europe, established separate systems for farmers, e.g., France, Germany, and Luxembourg, though some of them only for smallholders (e.g., Italy and Portugal).
- Other countries define farmers, especially big ones, as self-employed and include them in general schemes for the self-employed.
- Other countries include farmers in even more comprehensive schemes that cater to the entire economically active population, i.e., employees and self-employed.
- The broadest inclusion is reached when farmers are included, as all other citizens, in a universal scheme. This may be based purely on citizenship and financed out of taxes as in Denmark (where the scheme was originally means-tested) and, like in the Netherlands, it can be a "people's insurance" based on contributions.
- Finally, the distinction between separate and more universal schemes may be blurred if people are included in a general scheme but are subject to special regulations applying only to their group. In the PRC at present, few schemes exist where farmers could be integrated. The urban scheme mainly refers to employees but farmers are not employed. There are no wages that could serve as contribution base and no employers that could contribute either.

Thus, the question of including farmers raises more general questions about the future shape of social security in the whole country. While the possibility of a nationwide scheme with universal coverage and eligibility is not even discussed, foreign experience could suggest to consider a scheme for the self-employed. Self-employed, small or big entrepreneurs, are a key

factor of economic modernization in the PRC, and may even become more important in the future. If some sort of insurance were set up for them or if they were to be included in other schemes (as planned for the urban workers' scheme), the farmers might be included as well. But problems remain because the business of farmers is closely intertwined with production for subsistence and it is difficult to fix contributions in monetary terms.

Though a universal insurance or provision scheme is not likely to be established, we must recall that the Minimum Living Standard System has a universal character. It is the first universal social security scheme in the PRC even if eligibility is based on need. This shows that the idea of universalism is not entirely alien to the PRC social policy.

An integrated, more comprehensive scheme is not necessarily better than a separate scheme for special groups. It depends on the institutional design. A higher level of integration, tending toward universalism, avoids exclusion of certain groups that may, though not necessarily, be a consequence of categorical schemes that only aim at distinct groups (see the next section on equity and exclusion). The choice between separation and integration is not absolute, there are in-between solutions, namely integrating farmers into more general schemes while retaining special regulations for them. Such a model leaves future developments open and allows for adaptation to changing circumstances.

Another in-between solution is to set up separate schemes that operate on similar rules and might become more similar in years to come. An example of this version is the German social insurance with its separate branches for white-collar and blue-collar employees. While till the 1950s both systems differed markedly, with pressure by the trade unions to upgrade blue-collar scheme to the standard of the white-collar one, they have been gradually adapted to each other since, so that today benefits and regulations are almost identical.

The main lesson regarding the issue of unification is that the question of how to include farmers in old-age security cannot be tackled without thinking about the institutional design, the divisions, and the values incorporated in the overall social security—an integrated approach as described in Chapter 3.C (Table 8 and boxes 1 and 2).

2. Inclusions and Exclusions—Questions of Equity

The category "farmers" is heterogeneous, it can have many meanings. If farmers are covered by a universal scheme this issue is less pressing although there may be different provisions for different types of farmers even under a universal scheme. If farmers are included in less than universal schemes, however, there is a wide range of possibilities whom to include and whom to exclude. "Farmer" may mean the following.

- The male farmer as owner or leaseholder is the core population addressed by pension schemes.
- Smallholders are treated differently from big farmers in some systems, especially in Mediterranean countries like Italy, Portugal (where the separate systems for small and big farmers were united at a later stage), and Spain. These countries started with the inclusion of smallholders for whom need is obviously more urgent.
- Employed farmworkers may also be treated differently. In Germany, for example, they do not belong to the separate system for farmers (except for accident insurance) but are included in the general scheme for employees. This may imply a discrimination because there are fewer subsidies in the general scheme.

- Family members working in farming on a noncontractual base—wives, children, and relatives—are included in most systems.
- Wives of farmers and farming women are treated in various ways in different countries (Box 4).
- Survivors: Widows (and widowers and orphans).
- Seasonal workers and migrants.

The picture of inclusion and exclusion differs among the European countries. In the United Kingdom, for example, both the employed and the self-employed are members of the general system but they are treated differently, while noncontractual family workers may join on a voluntary basis. The overall trend is to include more and more of the above-mentioned groups although, for example, the Irish scheme of 1988 allows noncontractual family workers not even to join voluntarily.

For the PRC, all these groups raise issues of inclusion, with the exception of owners and large leaseholders who do not exist. The treatment of these different groups currently seems to be a sleeping issue, but we may expect that with increasing education and aspirations among farmers, questions of equity will soon be on the political agenda. Two issues stand out already: How to include women and how to include the poor (Boxes 5 and 6). In Chapter 5.C, it will be shown that women are sometimes discriminated in the organization of agriculture and rural social security. The inclusion of the poorest farmers obviously is a problem that can be seen from the low take-up of the pilot pension schemes introduced in the 1990s.

Box 5: How to Include Women?

In the context of rural social security, women are addressed in three social roles, correspond to three types of entitlement. These are graded from full inclusion to subsidiary inclusion:

- When women can build up entitlements to benefits independent of their husbands, they are treated as full individuals, as farmers like male farmers.
- If women are only defined as wives and widows, they enjoy only entitlements derived from contributions and entitlements of their husbands.
- Defining a woman as wife may also imply covering her indirectly through benefits to male farmers that are related to family size, e.g., with higher benefits for married farmers.

In addition, women may be totally excluded from social security. Again, the picture among European countries is diverse (Winkler 1992): Denmark, the Netherlands, and Greece bestow equal and independent entitlements, the first two countries even if women do not work in agriculture. This is due to the universal character of their security systems or, in the case of Greece, due to the noncontributory character of the scheme. In France, Italy, Luxembourg, Portugal, and Spain wives are compulsorily insured with independent entitlements if they work in agriculture, but benefits are lower. The situation in the United Kingdom is similar though the status of entitlements is a rather derived one. In Belgium, Germany, and Ireland, women cannot acquire independent entitlements but can only share in family size-related benefits received by their husbands. If a woman is legally the owner or leaseholder, she can participate in these schemes like men but this condition is rarely fulfilled.

Box 6: How to Include the Poor?

The lesson to be learned from European countries is that the low incomes of farmers require a high degree of redistribution and state subsidies to pension schemes. Although most European schemes are contribution-based, they are less earnings-related than ordinary social insurance for employees. In Greece, benefits are even entirely unrelated to the working biography of a pensioner.

Fully earnings-related benefits, in public or private schemes based on individual accounts, cannot adequately cater to the poor. In the current pilot schemes in rural PRC, this shows through nonparticipation or extremely low contributions made by poor farmers.

For this reason some European countries have established minimum pensions within their scheme, for example in Italy and, gradually building up from 1974, in Spain. These minimum benefits, however, are rarely entirely unconditional. Generally, benefits in farmers' schemes tend to be low, designed only to complement other sources of income, mainly family support, for example based on rural generational contracts like the "elderlys' share" in Germany. All in all many farmers' schemes are close to uniform flat rate pensions, for example explicitly so in Greece.

3. Finance

As mentioned earlier, although most schemes are contribution-based, in all of them there is a subsidy from government. The first and key lesson therefore is that massive government subsidies to farmers' pensions cannot be avoided. These subsidies can make up as much as 70% of total spending (in Germany) and result from the decreasing numbers and the ageing of the rural population that prevent both public and private schemes to operate in the usual way.

However, subsidies may take on many forms. Two key questions are, where do subsidies go to and from which source do they come?

Subsidies can either go to benefits or to contributions, i.e., they may enter at different stages of the operation of the scheme. This difference matters even if at a given time the size of the subsidy may be identical. There are good reasons to subsidize contributions rather than benefits. The subsidies paid by local semigovernments under the PRC pilot schemes do go to contributions, but in a more extended scheme, the system of subsidies would have to be refined. There are three reasons for subsidizing contributions.

- Such subsidies retain the idea of individual accounts, either real or notional, and thus link up with the idea of self-reliance.
- Subsidies to contributions are more visible than just filling up certain level of benefits. So subsidies can be more justifiably identified and more easily be controlled and changed. The Korean model of subsidizing two thirds of contributions (to be phased out by 2006) provides an example. Subsidies can also be targeted more precisely and differentiated by group, e.g., if cadres could get higher subsidies.
- When the system becomes more complex like in Germany, contributions may be subsidized by different agencies for different times and for different reasons of lacking income. In case of unemployment, for instance, contributions to old-age pensions could be paid by the unemployment benefit authority. In this way responsibilities could clearly be attributed.

If there is a minimum benefit a subsidy to benefits is required but through sufficient subsidies to contributions the need for such subsidies is reduced.

It is a reasonable aim to minimize the use of taxes for subsidizing social security. But there are choices among different forms, and they make a difference. European systems mainly rely on four sources.

- General tax revenue: In this case it matters from which departmental budget the money is taken because it competes with other items of that ministry, e.g., Ministry of Labour, Ministry of Civil Affairs, Ministry of Finance, or Ministry of Agriculture. In the latter case the money may be counted not as social spending but as agricultural spending and may thus get more political support.
- Consumer tax on agricultural products, as in Greece, might appear as an obvious source. In this way urban citizens would support farmers. This might be seen as fair and just. Opening the market for agricultural products to international competition under the World Trade Organization, however, might preclude this option.
- A special tax akin to an ear-marked income tax supplement is levied in Greece (along with a consumer tax and general state subsidies). In the Greek system there are no contributions by participants at all. Denmark has an income tax supplement as one source of general revenue for its universal scheme.
- Redistribution among the contributors of the insurance scheme is an alternative to taxes. Better-off contributors would then subsidize poorer farmers, as in some European countries. The willingness of other contributors to do so may be limited though it also depends on how visible redistribution is.

Other ways of financing subsidies may be available in the PRC context, such as selling state assets. Despite subsidies, contributions still are a major source for farmers' pensions in European countries. So we need to know what is the contribution base, how is the amount of contributions that a person has to pay defined with regard to the economic situation of that person.

For the current pilot schemes in rural PRC, this is no question since participation is voluntary and the amount of contributions to be paid is also up to the individual. It is a scheme without defined contributions and also without defined benefits, without a specific pension level to be reached. If a pension scheme goes beyond this simple model of organized saving, the seemingly technical question of how to define the contribution base becomes more urgent for three reasons.

- If the scheme should be run on a pay-as-you-go basis, the underlying generational contract involves reciprocity of giving and receiving. What is given, therefore, needs to be fixed according to equitable criteria.
- If participation in a system, public or private, is compulsory and there is a certain objective regarding the level of benefits in old age, the contribution rate also has to be determined.
- If a system involves a degree of redistribution, e.g., by establishing a minimum pension, criteria of eligibility have to be defined, normally referring to years and (absolute or relative) level of contributions.

The European schemes define the contribution base in very different ways (Winkler 1992). The following have been chosen as basis of assessing contributions:

- gross taxable money income, chosen in Belgium, Britain, Ireland, Luxembourg, Netherlands, and partially in France;
- the capital value of the farm or the farm land, chosen in Italy and partially in France;
- a percentage of a fixed amount, e.g., in Spain;
- a percentage of minimum wage in agriculture or in wider sectors of the economy; this alternative was chosen in Portugal and, for the mandatory second layer, in Greece; and
- in Germany a basic amount of contributions is fixed by government regulation but subsidies are paid according to income so that in effect income is the contribution base.

On the issue of contribution base there are no immediate lessons to be learned for the PRC since this base depends very much on specific social and economic conditions of a country. However, it can be said that money income as a base may not be useful for present-day PRC because there is a substantial proportion of subsistence or natural income. This might lead to the idea of drawing on natural sources as contribution, for example a share of agricultural produce or labor given by farmers to government development projects (Gillion et al. 2000). To allow for regional diversity, a certain amount may be fixed but with a varying percentage to be paid according to area or to the individual household. However, no solution will do full justice to the diversity of living situations. Moreover, contribution evasion cannot normally be avoided altogether. Under the Chilean system, workers try to minimize their income declaration to become eligible for special benefits.

4. Beyond Cash Benefits

Pension policy is not only about cash, contributions, subsidies, financial calculations, demographic ratios, and investment of funds. Pensions are embedded in people's lives. The attitudes and life plans of individuals are important parameters in operating the system. In some European countries, for example in Germany, farmers pensions are part of a more comprehensive package of social security that includes accident insurance, health insurance, early retirement, and also measures of rehabilitation. Accidents and ill health are pressing issues in present-day PRC, too.

There is another issue missed in the PRC debate, namely the need for counseling and advice for farmers. Rural advice centers are a comparatively cheap way of providing services that may have a considerable impact on people's lives. Advice centers exist or are called for in several areas, e.g., for the disabled, but they have not yet been considered for rural pensions. Since farmers are on average less educated, there is a specific need in rural areas, both for old farmers when they reach pensionable age and for young farmers who are planning to provide for old age (Boxes 6 and 7).

Box 7: Beyond Cash Benefits—A Case for Rural Advice Centers

Pensions are not only about paying, calculating, and investing money. There is a case to provide counseling to farmers. Counseling is normally only considered for personal social services in fields like health and psychotherapy, but cash benefits that affect the life plans of citizens as pensions do can and should be supported by an institutional environment that provides individual guidance.

Counseling and advice may be given on diverse areas related to pensions. It may be needed in particular at critical passages or transitions in the life course such as setting up a family or reaching pensionable age. Advice may be given on

- how to set up a formal or informal contract between a farmer who wants to retire and his children;
- how to coordinate working on one's own land and working in a TVE;
- how to choose between different options of public and private insurance for old age, health, accident, and other contingencies;
- how to afford education for the children;
- how to take up public benefits (information, encouragement); and
- agricultural advice: how to improve farming, use recent technologies, cooperate with other farmers, etc.

In face-to-face talks with a professional counselor, farmers and their families can address economic and personal problems that arise within the household. This may also be a way of strengthening the position of weak members of the family, mainly women and children.

Advice centers can be run by government; by self-organized associations (which might be supported by government) like farmers' associations, women's associations, or elderly associations; and by nongovernmental organizations (NGOs), either group-related like United Nations Children's Fund (UNICEF) or general developmental NGOs. Misereor, the Roman Catholic aid organization, for instance, is supporting legal advice centers in the countryside.

Box 8: Rural Advice Centers—The German Experience

Counseling and advice for farmers rest on three pillars: special branches of the agricultural authorities reaching to the level of districts and counties; local branches of the German farmers' association; and, from the late 1980s, social counseling centers erected by the Roman Catholic or the Protestant churches.

The centers address economic problems that arise, e.g., from giving up farming or from indebtedness of the farm. They also address the specific stress that goes along with agricultural production and related social and psychological problems of farming families. Whereas the government centers focus on economic questions, the advice given by the farmers' association addresses the full range of issues, including, again, giving up farming or handing the farm over to the younger generation, income tax, and providing for old age. In practice the farmers' association works closely together with the government agricultural authorities and they supplement each other.

5. Beyond Social Policy: The Economic Use of Social Security

There is another, more important point, also missed in the PRC debate: the relationship between social policy on the one hand, and economic and agricultural policy on the other hand. The most important lesson from European history concerns this point. Governments pursue social security not only for moral and social reasons but also for economic reasons. Social policy does not just mean giving to the weak but, as described in Chapter 3.A for pensions, it can also be a rational instrument of economic policy. In Europe a key objective of old-age pensions for farmers, besides their welfare function, has always been and still is the development of the rural economy.

Pensions in the modern sense establish an age threshold, a dividing line between workers and nonworkers. They introduce the notion of retirement that did not exist in rural areas and, more generally, in premodern societies. Retirement is an institution of modern society. It is a social institution but it is also an instrument for regulating the labor market (see Chapter 3.A).

It is clear that economic policy has implications for social policy. In a growing economy, wages will rise, the standard of living of the people will be lifted, and state revenue will increase. Therefore, it makes sense to give priority, as done in the PRC, to general economic and agricultural policy as compared with cash transfers. Likewise, Article 39 of the Treaty of The Common Market of the European Union explicitly states that agricultural policy also aims at improving the living standard of the rural population. The point here is that it also works the other way round: Social policy can be an instrument of economic policy. The two main economic functions of pensions and retirement are raising the productivity of agriculture and regulating the labor market (for European evidence see Winkler 1992).

a. The Economic Use of Pensions I: Raising the Productivity of Agriculture

The introduction of pensions for farmers can promote the modernization of agriculture by supporting structural changes toward increased productivity and downsizing. This includes the introduction of new technologies, new strategies of growing and selling, and other forms of modernization.

In European countries, this aim was pursued by tying pensions to a change in the management of the farm: Farmers can receive a pension only if they give up farming. This requirement is a part of German and French laws and in many other countries. Farmers who want to retire have two options.

- They may either give up their farm entirely if it is unproductive and unprofitable, or, under German law, may lease it to somebody else for at least nine years.
- Or they may hand over the farm to the younger generation that can be expected to be more open to new methods of growing and making business. The younger people might also consolidate small farms into bigger units, combined with a reduction in the labor force.

In Germany, in addition to the general scheme, there is a special scheme aimed at encouraging retirement as early as the age of 55 years. This version, enacted in 1989 (Lampert 1998), is even called "Giving-Up-Production-Pension."

If the PRC should opt for full-fledged commercialization of agriculture, then old-age pensions would be, following the European example, a major instrument to support this process. In fact, the pressure to introduce pensions is likely to become overwhelming in the next 10 to 20 years, so that it makes sense to prepare for the future now.

b. The Economic Use of Pensions II: Regulating the Labor Market

Through compulsory retirement, pensions may also be an instrument of reducing labor supply and helping cut the rural surplus labor.

This can be seen from those European countries that not only require pensioners to give up farming but even require them to do without any kind of employment or self-employment. This is the case in Spain, in the United Kingdom (employment not allowed at the age of 70) and, in case of retirement between 60 and 65, in Luxembourg. Other countries at least encourage giving up any gainful employment or self-employment. In these countries any additional income of pensioners will lead to reductions of their pension. This is the case in Belgium, Italy, and Portugal and, between the ages of 67 and 69, also in Denmark. In Italy, Portugal, and Spain the minimum pension is means-tested.

In present-day PRC, the opposite strategy is pursued: Farmers are encouraged to work in old age. It is also a custom in rural areas. But it does not equally apply to all areas and it seems to be declining. In the field visits we found that only in very poor areas did people actually work till they died or were entirely incapacitated. In better-off areas people gave up work in their late 60s or at the age of 70.

The commercialization of agriculture, if fully pursued, will entail a huge reallocation of labour force and unemployment. The policy of limiting commercialization is also a strategy to avoid mass unemployment. But when commercialization expands, pensions can serve to regulate the labor market.

c. The Case of East Germany

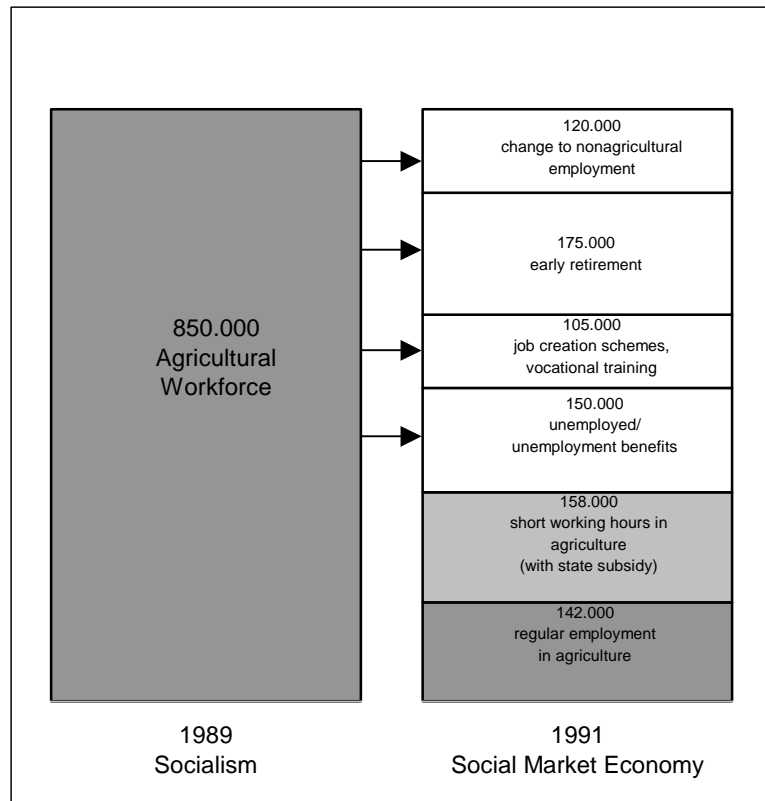
The economic use of social security goes beyond pensions. This can be seen in the case of communist East Germany, which was united with capitalist West Germany in 1990. The link between economic and social policies in this process may seem remote to the PRC but reality might put similar issues on the PRC agenda sooner than expected.

In 1990, East Germany also faced the task of transforming state socialism and reducing and restructuring a vastly unproductive agriculture. The East German economy may have been more developed than the PC but, unlike postreform the PRC, it was still riddled with the collectivist organization of farming. Figure 2 shows that within two years after unification, the agricultural labor force in East Germany was cut by 80%. How was this achieved without risking social instability and social protest? The bulk of surplus labor was absorbed by social security and other measures of social policy, mainly

- mass early retirement,
- public job creation schemes and vocational training set up by the Government,
- unemployment benefit for the openly unemployed, and
- short working hours allowance to support those farm laborers who worked short hours (which in reality often meant "short working hours zero").

Without this massive and very expensive use of social policy as an instrument of economic change (also in the industrial sector) German unification would most likely have failed (Leisering/Leibfried 1999). Modernization usually brings with it social dislocation and deprivation but social policy can be used to alleviate distress to ensure social stability. The East German transformation demonstrates the link between social and economic policies in a historical situation where social change unfolded even more rapidly than in the PRC.

**Figure 2: Transforming Socialist Agriculture through Social Policy
—The Case of East Germany**



Source: Hagedorn/Mehl 2001.

Chapter 5. FROM EAST TO WEST, FROM RICH TO POOR—THE COUNTIES VISITED

The team leader and the domestic expert visited four counties: Zhaoyuan City, Muping District, Wuding County, and Huangpi District. Due to different socioeconomic conditions, they belong to different administrative categories (city, district, county) but all of them are administrative units at the county level. Referring to them as a group, we, therefore, may speak of "counties."

The four counties represent a mix of rich, middle, and poor areas. In this Chapter we describe the economic, demographic, geographic, and social contexts for the pension development, comparing the counties with each other and locating them in their respective province and the whole country. Table 11 provides basic data.

Table 11: The Basic Data of Counties Visited
(2000)

The Counties Visited	Well-Off Counties		Poor County	Middle County
	Zhaoyuan City, Yantai Municipality, Shandong	Muping District, Yantai Municipality, Shandong	Wuding County, Chuxiong Autonomous Prefecture, Yunnan	Huangpi District, Wuhan Municipality, Hubei
Divisions of Administrative Areas	14 towns, 724 administrative villages, 729 natural villages	10 towns, 3 townships, 608 administrative villages, 711 natural villages	10 townships, 3 towns, 128 administrative villages; 1,915 natural villages	13 towns, 2 townships, 607 administrative villages, no data available for natural villages
Total Population (1,000 persons)	577	497	260 (half of them from 20 ethnic groups)	1,100
Rural Population (%)	81.0	81.0	94.8	83.0
TVE Employees (% of rural working population)	36.4	36.1	12.5	48.0 (including employees in household unions and individual households)
Per Capita Net Income of Rural Households (yuan)	3,900	3,377	1,368	2,600
Current Minimum Living Standard in Rural Areas (yuan/year)	600 (available since 1996)	580 (available since 1996)	(not available yet)	600 (only available from August 1997 to March 1999)

Source: Our group interviews with the related government bureaus in the chosen counties on the 9, 11, 16, and 22 May 2001.

A. Economic Development

Shandong, Hubei, and Yunnan stand as exemplary provinces of the Eastern, Middle, and Western Regions in the PRC, respectively, corresponding to different levels of economic development.

Both Zhaoyuan and Muping, as administrative areas of Yantai Municipality, are located on the Jiaodong peninsula, one of the five richest rural areas in the Eastern Region. The other four areas are the Liaodong Peninsula, the Beijing-Tianjin-Tangshan area, the Yangtse River delta, and the Pearl River delta. Third, Zhaoyuan City, one of the 427 cities at the county level in the PRC in 1999, is at least one of the richest counties in Yantai; and Muping District, one of the 749 districts at the county level in the whole country, is a middle-income county in Yantai.

Huangpi District of Wuhan Municipality, although one of the 749 districts, is a middle-income county in Hubei Province. Turning to Wuding County in Chuxiong Autonomous Prefecture, as its title implies, it is not a rich area. Wuding is one of the 63 nationally defined poor counties in the province, or one of the 594 poor counties in the whole country. The data on per capita net incomes of rural households in Tables 11 and 12 demonstrate the economic positions of the visited counties in their respective provinces and in the whole country.

Table 12: Per Capita Net Incomes of Rural Households by Region
(yuan)

Region		1998	1999	2000
National Average		2,161.98	2,210.34	
Shandong	Total	2,452.83	2,549.58	
	Zhaoyuan			3,900
	Muping			3,377
Yunnan	Total	1,387.25	1,437.63	
	Wuding			1,368
Hubei	Total	2,172.24	2,217.08	
	Huangpi			2,600

Source: National and provincial data from the National Bureau of Statistics, local data from the interviews.

B. Demography

Table 11 shows the proportion of rural population in the chosen counties and Table 13 shows the proportion of older people in the provinces and counties. Generally, we can assume that economic development is a major determinant of both demographic variables.

Local regulations on family planning and their enforcement could also have contributed to demographic conditions. According to the State Family Planning Commission (SFPC), Shandong, along with Beijing, Heilongjiang, Jiangsu, Jilin, Liaoning, Shanghai, Sichuan, Tianjin, and Zhejiang, and, is one of the 10 best provinces implementing the family planning policy. Their fertility rates are fairly low and stable. By contrast, Yunnan, along with Guizhou, Hainan, Ningxia, Qinghai, and Xinjiang, are rather backward with regard to the policy. In between the two groups, there are Hubei and other provinces such as Guangdong. Their fertility rates are fairly low but not stable yet.

Table 13: Proportion of Elderly in the Selected Counties and Regions in Recent Years (%)

		Proportion of Elderly Aged 60+	Proportion of Elderly Aged 65+
National	Total Population	11.11	7.43
	City	12.09	7.41
	Town	11.03	7.15
	County	9.96	6.73
Shandong	Total		8.6
	Zhaoyuan	14.9	
	Muping	14.0	
Yunnan	Total	10.1	6.0
	Wuding	9.0	
Hubei	Total	10.24	7.1
	Huangpi		5.9

Sources: National data from NBC Population, Social and Science Department, and local data from the interviews with localities concerned.

C. Geography

Among the four counties, Zhaoyuan and Muping are hilly and Wuding is mountainous. Huangpi is located in the Yangtze-Han plain. Geographic features not only strongly impact on local economic development but also on the operating cost of local pension schemes.

From the difference between the number of administrative villages and the number of natural villages in a county, we can tell its basic geographic feature. Generally, a county is mountainous if there are much more natural than administrative villages. If people live concentrated in few villages, it will be convenient for executive agencies to collect contributions and pay out benefits.

D. Social Support Measures for the Elderly

Clearly, old-age pensions are not the only, not even the most important support directed at the rural elderly. Local governments at various levels in the chosen areas have launched legal campaigns to urge children to support their elderly parents. Following the related guidelines from the Centre, they have also adopted various other policy measures to protect the rural elderly (Table 14).

- A new means of consolidating family support, which puts children under a legal contract to look after their elderly parents.
- Traditional arrangements such as the Five-Guarantees program and community assistance. More than 95% of the recipients of the former benefit are older people who have no children, no income sources, and have lost their working capacities.
- Two measures to relieve older people from such burden as unpaid community jobs and various fees charged by both the village committee and the town/township government.
- Two social assistance programs. One is the Minimum Living Standard System (MLSS), which provides cash benefits for absolutely poor households. Another is the social mutual aid program, or hand-in-hand program, which calls for various assistance such as money, goods, labor, information, technology, etc., to poor households from individual government

departments, enterprises, party members, and cadres at the grass roots, and rich households. Those volunteers should establish one-on-one relationship with certain poor households to help them achieve net incomes equivalent to local averages in a few years' time.

Table 14 shows that these programs are not evenly developed in the visited areas. Once again, the introduction and upgrading of various programs depends on local economic conditions.

Table 14: Social Support Programs for Older People in the Counties Visited

Policy Measure	Zhaoyuan	Muping	Wuding	Huangpi
Contracted family support	Available in recent years to make children, especially sons, provide grain, cash, and care to their old parents	Available in recent years to make children, especially sons, to provide grain, cash, and care to their old parents	Not mentioned	Not mentioned
Reduction of or exemption from community jobs	Available since 1998 for those aged 60+	Available since 1998 for those aged 60+	Available for those aged 60+ in recent years	Available since 1998 for those aged 60+
Reduction of or exemption from fees	Available since 1998 for older people, especially those aged 70+	Available since 1998 for older people, especially those aged 70+	Available since 1998 for older people, especially aged 80+	Available since 1998 for older people, especially aged 65+
Five-Guarantees (state/collective support)	Available in case of Three-No's (benefits equivalent to 2/3 of community net incomes)	Available in case of Three-No's (benefits equivalent to 2/3 of community net incomes)	Available in case of Three-No's	Available in case of Three-No's at 1,000 yuan annually)
Community (neighborhood) assistance	Available	Available	Available	Available
Social mutual aid program	Available since 1995 for relatively poor households	Available since 1995 for relatively poor households	Temporary assistance available, e.g., helping harvest; institutionalized program: not mentioned	Not mentioned
Minimum Living Standard System in rural areas	Available since 1996 for absolutely poor households	Available since 1996 for absolutely poor households	Not available	Available only between August 1997 and March 1999

Sources: Interviews in the chosen counties.

Chapter 6. KEY ISSUES OF REFORM

The key issues of reform include the viability of the traditional forms of support for the elderly (Chapter 6.A) and of the new public pension schemes (section B), social exclusion and inclusion in the changing PRC countryside (section C), the economic and political environment of old-age security systems (section D) and the more recent idea of a leading role of commercial provisions for old age (section E).

A. Can Family and Land Still Provide for Old Age?

The purpose of this section is

- to describe the traditional security system for dealing with support in old age and mishaps and contingencies such as major illnesses, and
- to show how socioeconomic changes seen in recent years have weakened the traditional system and created the need for a new arrangement.

The traditional security system in the PRC countryside is based on the family and the land plot it owns. The land plot provides the means to employ family labor, thereby yielding products for own consumption and for sale. If land is sufficient, the family's prosperity depends on working members relative to the number of dependents. If land is insufficient to generate enough income, some family members have to seek outside employment. With the cultivated land area fixed or declining and a rising rural population, the latter is increasingly the norm.

1. Family Support: Its Structural Problems

Security in the sense of dealing with mishaps, such as illness and death, and support in old age depends on the sharing of income and of mutual help. Close family members living in the same household or in close vicinity share income, including production for own consumption. The extended family provides the second line of defense against risks that are beyond the capacity of the immediate family to handle. The kin group and neighbors constitute the last line of defense. This multitiered security system suffers from problems but functions reasonably well under certain conditions.

First, the system is based on a small number of people. It can be effective in dealing with risks that adversely affect only a few individuals at one time. Because the system provides a limited risk pooling, it is not good at dealing with risks that affect the whole family. Similarly, mutual help among extended family and the community coping with adverse events may fail to work when these affect the whole group. Examples of such adverse events include natural disasters. Related to the above, the traditional system does not provide protection against poverty affecting the whole family and the community.

Second, the extent to which income is shared among family members depends on co-residence in the same household or in close vicinity. Although income can be and is shared among close members living apart, such as parents and children, the splitting of families due to, for example, migration dilutes the extent of the sharing of income and consumption. This assumes a particular importance because of increasing migration.

About 90 million of rural population have recently migrated from rural to urban areas. The first agricultural survey found that some 8% or 45 million of the rural labor force were working outside their permanent living places for more than three months in 1996.

Third, mutual help within community is founded upon bonds of trust and acquaintance formed over a long time. Such mutual help does not work well in communities with a changing membership. Emigration and immigration of outsiders weaken the network of mutual help.

Fourth, family relationships are prone to conflict. Parents may not want to obligate their children to support them to preserve a degree of autonomy and avoid conflicts that are common in parent-children relationships (Box 9). If family support is given priority over public pensions, the social cost of this option must be acknowledged.

Box 9: Family Support May Breed Conflict

A three-generation household in remote Huapo Village, Wuding County, Yunnan

A young farmer, aged 35, has two children, aged 2 and 8 years, all lives with his parents. From his land, his only source of living, he can just secure subsistence by growing corn. He has no savings, no commercial insurance, no bank account, and virtually no expectation of a pension in old age (having made a tiny one-time payment for the public pension scheme). He thinks of a bank only with regard to loans. He sometimes took a small loan that usually takes him years to pay off. He also finds it difficult to pay the education for his children.

Recently his wife committed suicide. The reason was that: it is customary in the area that both parents go to live with one of their sons in old age. Only if the parents are ill will, each parent get to live with a different son. Although the 72-year-old father of the man has 7 children he, and his wife went to live with this son. An older son only buys shoes for the father occasionally. Under these circumstances a conflict between the wife and her parents-in-law arose. The parents could only work little but, as the man told us, they ate a lot. The wife eventually felt no longer able to carry that burden. The funeral left the family with a debt of 4,000 yuan, a loan from relatives. It can be concluded that parents may be a burden to their children and that pensions would be ideal.

Under conditions of severe poverty, even very basic family support is not self-evident and can be difficult to maintain. The relationship in a multigenerational household, if burdened with support obligations, may give rise to social conflicts that may have serious repercussions. Often the victims are women. Generally the suicide rate among women in rural PRC is extremely high.

The kind of family support provided and the inherent problems depend much on customs. If the burden for caring for the old parents had been shared among the sons, the tragic event may not have occurred.

The forms of family support and coresidence of families vary greatly, not only with regard to their capacity of support but also with regard to the potential of conflict (Box 10). High support capacity may go together with a high conflict potential. Policies cannot and should not influence the forms of coresidence. This is another limitation of a welfare policy that builds on family support.

Box 10: Forms of Coresidence and Family Conflict

Results of an unpublished study of the Old People's Association, Hubei Province

The survey found five key forms of family support:

- Coresidence of elderly and children (26% of elderly);
- core family: children live apart from their parents but retain close relationships that increase with age (30%)
- shared family support: several children support their parents, by money, grain or other help (36%); there are three subtypes: shared distant support; elderly going round to live with children, and each child supporting one parent;
- public support (Five Guarantees) in the absence of children (6%); and
- older people living with a child that never married or is widowed (2%).

Interestingly, not the first but the third type is most conflict-ridden, especially the relationship between daughter and mother-in-law and between son and father-in-law. The Old People's Association does not favor the support of one parent by one child because this system splits the old couple. However, taking in both parents may be a heavy burden on a poor family producing considerable tension between the generations (Box 9).

Conflict increases because younger people consider support less an obligation than before, and because their jobs have become more demanding, leaving them less time and energy to look after their parents.

Fifth, among some ethnic minorities family support is not a customary way of providing for old age (Box 11). Again, this testifies to the cultural diversity of family life. Welfare policy cannot rely on the family.

Box 11: Ethnic Minorities: No Tradition of Support for Parents among the Miao People

A very old Miao woman, in remote Huapo Village, Wuding County, Yunnan

She is 84 years old, like her husband who is very ill and unable to work (he worked till the age of 79). Although they have two sons and three daughters they get no support from their children whatsoever. This is the custom among the Miao people because parent do not want to be a burden to her children. The interviewee said that, even lacking reciprocity she sometimes looked after her grandchildren. Children do help their parents if they become severely ill and are totally incapacitated. In such a case the two sons would help her with food, but not with medical treatment. But normally she works even when she is ill. Through her work she also supports her husband. She grows corn like everybody in the village, additionally raising 3 pigs and 20 chicken. She is absolutely poor, without any savings and no money to pay a medical doctor to treat her husband.

Family support cannot be taken for granted. The Miao custom of non-support may be seen as an evolutionary response to the problems of family support under extreme poverty.

1. The Impact of Ageing and Migration on Family Support—A Macro View

Currently financial support for the elderly population in the whole country is split between families and the "society" (which in the PRC means the government and work units), with the former carrying the main burden. Taking 60 as the benchmark retirement age,⁶ only 37.3 million (26.6%) of the 140 million aged over 60 receive pensions and all but a small percentage of these are in urban areas. The remaining 73% are mostly rural residents dependent on their children, predominantly sons, for financial support. Public pension schemes in rural areas cover only a very small number of the rural elderly and mostly provide only a percentage of what is needed to cover minimum subsistence. In addition, there is also the Five Guarantees Scheme that provides assistance to the elderly, characterized by Three No's: no physical capacity to work, no relatives to depend on, and no savings. The scheme is not a substitute for family support. It covers only few cases where family support fails entirely.

The financial implications of the support of the elderly by their families has to be seen in the wider context of the age structure of the population that covers not only the elderly but also working-age adults and children. Table 15 shows the dependency ratios of the population in cities⁷ (with 22.7% of the population), towns (10.4% population share), and rural counties (66.9% population share).

Table 15: Dependency Ratios in the PRC Population, 1999

	Children/ WA Adults	Elderly/ WA Adults	Dependents/ WA Adults
Cities	25.0%	12.1%	37.2%
Towns	29.5%	11.2%	40.7%
Rural Counties	39.6%	10.8%	50.4%

Note: WA Adults refer to working-age adults aged 15 to 64.

Source: National Bureau of Statistics Department of Population, social, science and technology statistics (2000, tables. 1-7, 1-8, 1-9).

Following the usual convention, the category children covers those aged 0 to 14 and the elderly refers to those aged 65 and above. The ratios of children and of the elderly are expressed with respect to the working age adults. The number of the elderly per 100 working age adults varies between 11 and 12. The number of the elderly is highest in cities, followed by towns, and then in rural counties, but the differences are not large. These figures do not support the contention that at present ageing is only an urban problem. Though not large at present, the number of elderly per 100 working age adults will rise over time as the impact of the fertility decline feeds through the age structure.

At first sight the Table 15 suggests that the burden of old age support is higher in cities and towns relative to that in rural counties. This is the case if we focus only on the number of elderly per 100 working age adults. But that is a misleading index of the burden. The burden of support of the elderly has to be assessed in combination with the burden of supporting other

⁶ The current official retirement age in the PRC is low by international standards, ranging between 50 and 60. The actual retirement age is a distribution rather than a number and the choice of 60 as the benchmark retirement age does not affect the argument here.

⁷ Cities refer to the urban districts of cities, excluding towns and counties within administrative boundaries of cities. Data not adjusted for survey and sampling errors.

categories of dependents, in particular children. The lower percentage of the elderly in rural counties is more than offset by a higher percentage of children relative to the working age adults. As a result, the number of dependents (children and elderly taken together) per 100 working age adults is highest in rural counties and following that in towns. It is true that the cost of supporting children is different from that for the elderly, though not necessarily lower. The important point is that, relative to working age adults, the ratio of children is much higher than the corresponding ratio of the elderly, and the differences between the ratio of children between cities, towns, and rural counties far exceed those in the ratio of the elderly. As a result, taking into account the ratio of children, the burden of supporting the elderly population is higher in rural counties than in towns, which in turn is higher than in cities. The implication is that the argument for leaving the development of pensions for the rural population for the future because of a comparatively low percentage of the elderly is weak.

Social security schemes, in particular old-age pensions, involve commitments in the future. In relation to old-age pensions a crucial question is how would the age structure of the population change over time? Table 16 presents the dependency ratios of the population at the national level in 1999 and the projected structure in 2020.

Table 16: Dependency Ratios in the PRC Population, 1999 and 2020

	Children/ WA Adults	Elderly/ WA Adults	Dependents/ WA Adults
1999	35.0%	11.2	46.1%
2020	27.9%	16.5%	44.3%

Note: WA Adults refer to working-age adults aged 15 to 64.

Source: National Bureau of Statistics Department of Population, social, science and technology statistics (2000, Tables 1-6)

The age structure in cities, towns, and counties will depend not only on the national trend but also on the migration pattern. The likely trend in cities, towns, and rural counties is a rising ratio of the elderly in the population. But the rate of rise in cities and towns will depend not only a change in the age structure of the original population but also the age structure of immigrants from rural counties. Depending on the rate of immigration, the latter may outweigh the former. The current policy to raise the percentage of the urban population through the development and a relaxation of restriction on immigration to small and medium towns will lead to a reduction in the percentage of population in rural counties. Given that emigrants from the countryside consist largely of working age adults, emigration would raise the percentage of the elderly in the population remaining in rural counties. Depending on the rate of rural-to-urban migration, by 2020 the ratio of the elderly in the population in rural counties may well exceed those in towns and cities. The phenomenon of ageing through the exodus of the relatively young has been observed in a number of countries with a high rate of migration from rural to urban areas. The implication is that the planning of support for the elderly population has to be based on not only the birth and death rates but also on the pattern of migration.

What will be the impact of the composition of the dependent population is shown in Table 16 a fall in the number of children and the number of elderly per 100 working age adults. Taking the current arrangements for old-age support as given, the Government, enterprises, and families will all feel the financial impact of the rising elderly population. In urban areas the cost will fall mainly on work units (including their employees) and the Government. For the latter, with all

else held constant, it will be offset by the declining ratio of children, though not necessarily completely. State-owned units (including government and public organizations), which already carry a heavy burden of old-age pensions, will be most adversely affected by the trend. Currently, around 77% of retirees are ex-state sector employees and this percentage will rise over the next two decades because of the higher median age of the state-sector labor force compared with that of the nonstate sector. Given the high percentage of the urban elderly population receiving old-age pensions, urban households would feel the financial impact of the rising elderly population largely in the form of higher taxes (including social security contributions) rather than in the form of providing direct financial support for elderly parents. In contrast, rural households would feel the economic impact of the changing age structure largely through expenditure on children and elderly relatives. With the development and extension of rural public pension schemes, part of the cost will be shifted to the community or to local government, showing up as contributions to the pension schemes or local taxes.

2. The Impact of Ageing and Migration on Family Support—A Micro View

The purposes of this section are to, first, outline the salient aspects of the support of the elderly by their children and, second, to outline how such support is affected by demographic trends, such as the ratio of the elderly in the population and population migration.

Dependence of the elderly on their children can be regarded as a small-scale “pay-as-you-go” (PAYG) pension scheme because of its following principal feature. For their support the elderly depend not on the savings accumulated in their working life but on the income of their working children, predominantly their sons. In practice the situation is more complicated than this. In many cases the elderly have savings and have property, principally houses, to pass on to their children. Further, unlike in the case of pension, support may be partly in the form of the payment for expenses and partly in the form of cash. In the countryside support is often combined with the elderly living with their children or in close vicinity. As a result, support partially takes the form of shared consumption.

Leaving aside various complications and just focusing on the support of the elderly by their working children, the support that the elderly receive depends closely on the income of their working children. The standard of living of the elderly is tied to the standard of living of their working children. Poverty of working children is necessarily reflected in the poverty of their parents. As a result, dependence of the elderly on their children often means a percentage of the elderly live below the poverty line. In developed economies prior to the introduction of pension system covering the whole population, the incidence of poverty among the elderly was generally much higher than that in the rest of the population. Related to the risk of poverty in old age, fluctuations in incomes of working adults is necessarily transmitted as fluctuations in the living standard of their dependent parents.

People we interviewed confirmed that old people are more likely to be poorer than younger people although even in counties that possessed a broad range of data, precise figures on poverty in old age were often not available. A survey by the Chinese Centre of Gerontology (Qiao et al. 2000) suggests that more than a third of the rural elderly find it difficult or very difficult to balance income and expenditure.

A natural reaction to the risk of poverty and fluctuation in the living standard in old age is for parents to have more children than they would have if they look forward to an adequate pension in old age. The decision to opt for more children is magnified by the cultural norm of parents in their old age depending on their sons but not daughters.

A policy to limit the number of births to less than replacement rate of two children per couple has direct implications for the support of the elderly by their children. Generally, the average number of children per couple would be higher than two children per couple, even if couples limit themselves to one son each. The likely target for many couples would be more than one son because that does not provide adequate security in old age.

The general implication is that the private aim of depending on children for support in old age is in general inconsistent with the social aim of maintaining a stable population, which means a limit of around two children per couple. The inconsistency increases when the social aim is to rapidly decelerate the population growth to zero by limiting a substantial percentage of couples to only one child, as in the PRC. As often pointed out in the PRC, one child per couple may lead to a situation where a working couple would be required to support five dependents: their child, two elderly parents of the wife and two elderly parents of the husband. Such a situation may arise and pose a serious social problem of inadequate support for the elderly.

Apart from this, migration and preference away from multigenerational toward nuclear households erode the ground from complete dependence of the elderly on their children for support. A common form of rural-to-urban migration is the emigration of working age members leaving behind older family members. Thus a usual effect of migration is the physical separation of close family members. To the extent shared consumption and living in the same household or in close vicinity lead to economies, the elderly living separately from their children raises the cost of support in old age. To this end one may add rising life expectancy which a lengthening of period in retirement.

3. Land as Support in Old Age

Traditionally land has been regarded in the countryside as the most reliable source of economic security. Following the reform of the rural economy, the collective land has been divided and allocated to rural households. Land remains under collective ownership, but households have long-term use rights on the plot allocated to them.

Apart from the practical and financial problems in extending social security schemes to the rural population, another reason for excluding the rural population is that rural households have each a plot of land that provides minimum level of income security. This raises the following questions.

- What percentage of the rural population actually has long-term usage rights on a plot of land and what is the likely trend?
- How much of economic security does the land plot actually provide?

In rural areas of Southern Jiangsu covering 12 counties⁸ (known as Sunan), according to a survey conducted in 1998, around 10.3% of households no longer possess land. Reasons include the conversion of agricultural land for nonfarm use and households giving up land so as to get out of the liability for the agricultural tax. Further, among 89.7% with a land plot, another 3% planned to give up their land plot in the near future. Southern Jiangsu is one of the richest rural areas in the PRC that is highly developed. But even in poorer rural regions, not all rural households have usage rights over a land plot. A 1999 survey of 1,500 households drawn from

⁸ These 12 counties include 6 within the administrative boundaries of Suzhou city and 3 each within the boundaries of Wuxi and Changzhou city.

15 nationally designated poor counties in Gansu and Inner Mongolia found that around 3% of rural households had no land. Not all rural households possess a land plot and among those who do, there appears to be a trend toward giving up land.

How much security does a land plot provide? The PRC's rural population is huge (860 million) and its cultivated area is limited: only 1.42 billion mu in total (Table 17, Box 12). As a result cultivated area per rural inhabitant is a mere 1.7 mu. The level of economic security that land plots provide to rural families varies very widely from locality to locality. More important, land plots are not sufficient to prevent poverty, not even extreme poverty. Most of the rural population with a per capita income less than 635 yuan per year, the national poverty line for rural inhabitants, have land. Unlike other developing countries "having land" and "not being poor" do not go together in the PRC.

Table 17: Cultivated Area in the PRC

Year	1952	1957	1965	1978	1987	1990	1995	1996 ^a
Cultivated Area (billion mu)	1.62	1.68	1.55	14.9	1.44	1.44	14.2	1.95
Rural Population (million ersons)	503	547	595	790	816	841	859	864
Per Capita Cultivated Area (mu/person)	3.22	3.07	2.61	1.89	1.76	1.71	1.66	2.26

^a The high 1996 figure on cultivated land is the result of the first agriculture survey, which includes actually used arable land and ditches, roads, and land on the slopes of more than 25 degrees.

Source: National Bureau of Statistics (1999) and NBS (2000: Table 12-1), NBS Department of Population, Social, Science and Technology Statistics (2000: Tables 4-5).

Box 12: Good Land is Becoming Scarce

Information by the Land Resource Department, Yunnan Province

Land is scarce. More land has been developed over the last five years but the new land tends to be of low quality. Unlike other provinces with more favorable natural conditions, few successful farmers are wanting to expand farming. New land is sometimes sought on steep slopes up to 25 degrees and beyond. Although such land may yield little, farmers risk their lives to work on slopes that, as we saw in the field visits, were dangerously steep. Moreover, obviously no cattle can be raised on such land nor buffaloes be used for ploughing. In Yunnan 90% of the land is mountainous. New land is also sought near cities. Still, land is not enough.

Changing patterns of behavior both reflect and accelerate the diminishing significance of land plots for the rural population. As a response to the scarcity of land and low yields, farmers increasingly seek other ways of providing for a living. Those who do not find alternatives are doomed to live close to survival. Increasingly, people also want to secure a living beyond mere survival, e.g., providing for cases of ill health by saving or contracting a commercial insurance, or by providing for times of incapacity to work due to accident (Box 13). They also want to spend money to further the education of their children.

Box 13: People Seek Alternatives to Land to Live Beyond Bare Subsistence

A young couple with two small children, working in a TVE brick factory, Jiuchang Township, Wuding County, Yunnan Province

They have left their land that is now tilled by their brother who is too old for switching to the TVE. They have a house in the village but the whole family lives in one room in the factory premises. Relying only on their land, they would earn 1,000 to 1,500 yuan per year. Deducting fees, spending on fertilizers, and subsistence nothing would be left. They could not save and not afford education for their children. Raising a pig or taking on a part-time job would be the only way to get some money income.

In the factory, by contrast, they earn 5,000 to 6,000 yuan per year (the man) and 2,000 to 3,000 yuan per year (the woman). This income enables them to save 4,000 Yuan per year and to pay 700 to 800 yuan per year for their children's schooling.

The village offers few opportunities. Their three-year-old house there could be sold, nobody wants it. Still, in old age they intend to return to live on their land in the village. They think of retiring at the age of 40 (!) because of the hard work in the factory. In old age they plan to live mainly on savings from their TVE wages that may in the future also be invested in a commercial pension if interest rates are high enough. They do not want to work on land during old age, but receive some supplementary support from their children if family relations are good enough.

The desire to lead a life beyond physical survival has driven this couple to leave their land. Even in old age, they do not want to work on the land but retire in the modern sense: land as a place of settling down in old age, not as source of subsistence.

More and more rural citizens are not farmers but work in TVEs or in other nonagricultural areas just like urban employees, especially civil servants, cadres, and people working in the service sector like shop assistants and small shop keepers (Chapters 6.C). TVEs employ 127 million workers, much more than the SOEs (85.7 million).

Living conditions and personal aspirations in the countryside are changing. Rising income sources that provide for mere survival are becoming less acceptable. Lifestyles are changing. Some people may not want land because they have different life plans (Box 14).

Box 14: Young People May Not Want Land

A young professional woman in rural Guanqianjiangjia Village, Zhaoyuan City, Yantai, Shandong

The 22-year-old woman has graduated from a professional high school and works as a cashier in an enterprise, earning 6,000 yuan per year. In her village, land is still collective but some villagers rent a plot. She herself does not want land, for three reasons

- She has no time to work on land since she is in full employment.
- She lacks agricultural skills.
- Also in old age, she will not need land since she is building up substantial pension entitlements. She pays an unusually high contribution of 1,200 yuan per year to the public scheme even though her employer provides no subsidy. She has no commercial insurance on top of that.

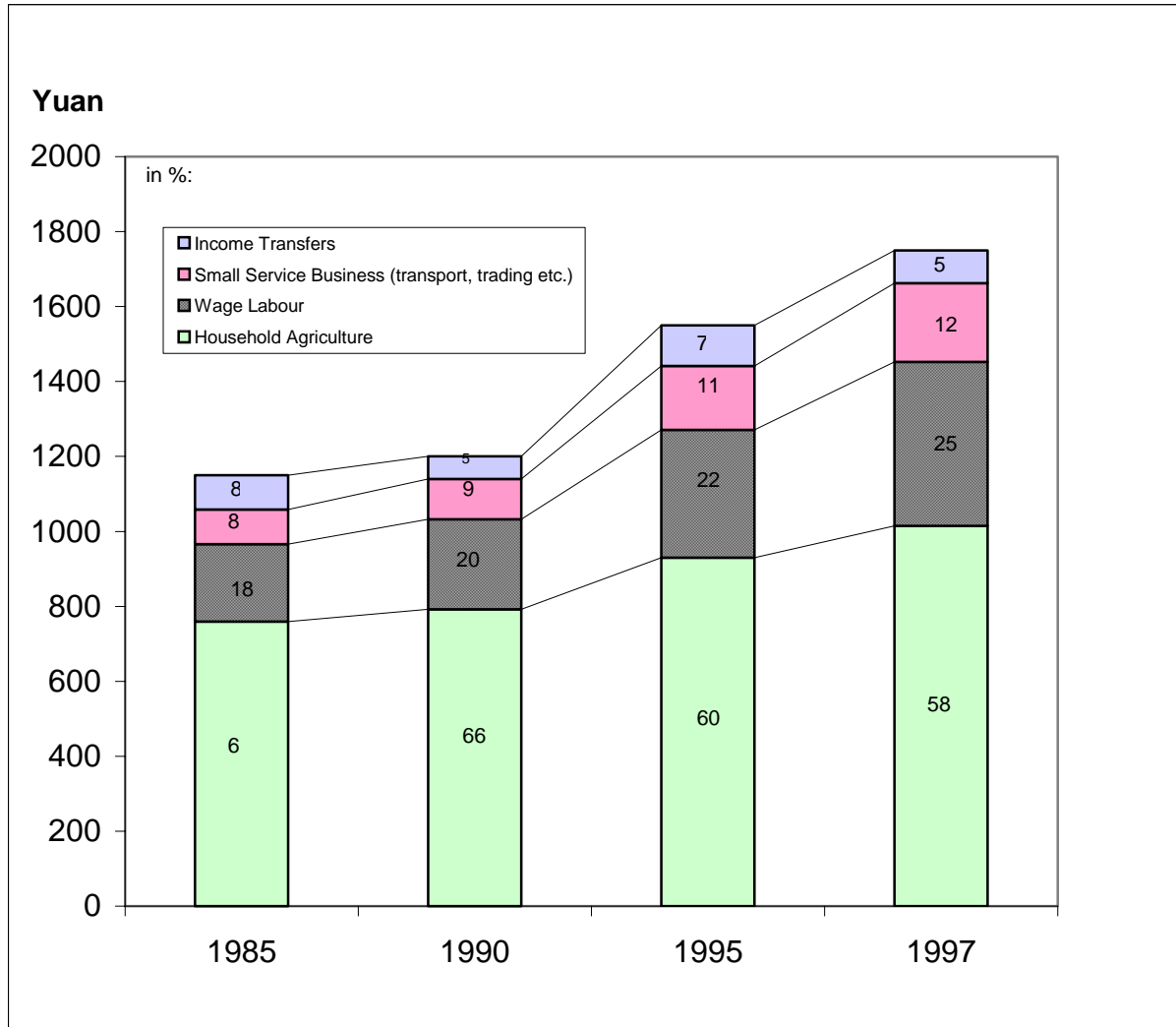
The young woman is adopting a modern lifestyle by replacing land with a public pension for old age. This case also demonstrates that a pension scheme for rural areas cannot be based on the assumption that rural citizens are farmers. This woman's employment does not differ from similar jobs done by urban citizens.

There is little doubt that the allocation of land to rural household has been an important source of economic security to the rural population. Without the allocation of land to all rural households, poverty in rural areas would have been much higher than it is now. Looking forward into the future, the level of economic security provided by land has been and will continue to diminish. With cultivated land area fixed, the gap between income from farming and income from industry and services has widened. The only way of arresting and eventually narrowing the gap is to consolidate land and increase the size of land-holdings. There is a conflict between maintaining the social welfare role of land, which requires dispersed distribution of land, and raising farm income, which requires a concentrated distribution of land. The conflict is going to become more pronounced and its resolution requires a gradual phasing out of the social welfare role of agricultural land.

4. Conclusion: Toward a New Welfare Mix

The general argument is that the traditional system of rural social security that is founded on the family and land is eroding. Declining fertility, population migration, and preference toward a nuclear family weaken the support of the elderly by their working children. On the other hand, economic changes diminish the importance of the social security role of land (Figure 3).

Figure 3: The Changing Rural Income Mix
(rural income by source 1985–1997, at constant prices of 1995)



Source: Nyberg/Rozelle (1999: 4, figure 1.2)

The decreasing importance of land is particularly apparent in rural areas where rural industry is well developed. In rural Sunan, income from farming on average accounts for around 20% of incomes of rural household. The percentage of income derived from farming varies across rural household. Households deriving more than 50% of income from land in rural Sunan tend to be either comparatively poor or rich household. Poor ones tend to be those with a small land plot and little nonagricultural income. Rich ones tend to be those households who specialize in farming and have managed to acquire additional land by means of leasing from the village or from other households.

In most cases family support and land are just components of a broader welfare mix so that it is misleading to simply say that farmers rely on family and land. This was an ideal but it matches reality less and less. In many cases, the income package of "farmers" is similar to that of urban citizens but nevertheless; they are not eligible to (urban) pensions that would make up for the reduced role of land and family support (Boxes 15 and 16). The changing welfare mix leaves a vacuum to be filled.

Box 15: Family Support and Land: Only Part of a Wider Income Mix (I)

An old man in Qianliuxing Village, downtown Zhaoyuan City, Yantai Municipality, Shandong

The man 61 is years of age, his wife 65 years. They have two sons and one daughter. Their incomes add up like this

- They grow peanuts and corn on their land.
- One son gives 500 to 600 yuan per year, well below poverty level, and the daughter makes voluntary contributions.
- The wife is ill and unable to work. Since her husband's resources are not sufficient, she receives an allowance of 200 yuan per year from the village.
- He receives a pension of 69 yuan per month while his wife has no pension.
- In the face of this low pension he still works, earning 300 Yuan per month as a gatekeeper on a government compound. He intends to continue working for another four to five years.
- He saves some money for future days when he might be unable to work.

The couple's income is a mix of diverse sources, pieced together from several small components. Family and land account only for a fraction of that package. This is typical for farmers who live in villages within cities. Due to the illness of the wife, the family aggravates the problems of securing an adequate income.

Box 16: Family Support and Land: Only Part of a Wider Income Mix (II)

An old man in rural Guanqianjiangjia Village, Zhaoyuan City, Yantai, Shandong

The man, aged 61, is married and with two children. The couple's income package adds up like this

- They use their land, which is 2 mu, to grow corn, wheat, and peanuts for subsistence. The wife also works on the land.
- Their son supports them with 100 yuan per month and gives more in case of illness. The daughter contributes irregular payments.
- He is still in paid employment as a security person for an enterprise, earning 400 yuan per month. The wage is paid annually because of cash flow problems in the company.
- He receives a pension of 110 yuan per month, which he collects at the bank immediately when it is transferred to his account because his wage is paid annually.
- Further, they have savings on a bank account to provide for contingencies like ill health.

Regarding the single components of the income package, this old couple is slightly better off than the one described in Box 15, but for them, too, family support and land are just a fraction of their overall income. There is a strong pressure for further sources of income: He intends to continue gainful employment as long as he can.

His work there does not differ from an urban employee but his pension does. The low level of his rural pension does not allow him to retire as employees under the urban pension scheme. Still, even this small pension is needed in the face of an annually paid wage. His main worry about his future is that the pension might no longer be paid due to financial crisis or due to changes in policies.

Public pension schemes are needed to fill the vacuum, and they have already started to do so. As Box 16 illustrated, even the small pensions under the pilot schemes are seized as a significant contribution to a household's income package. How would a bigger share of public pensions impact on the exchange relationships between the generations? Consider the introduction of a pay-as-you-go (PAYG) pension scheme in a rural area. What difference would it make for the support of the elderly?

In the case of family support for the elderly, the cost of support falls only on families with the elderly parents. Referring back to Table 15, there are currently 11 elderly per 100 working age adults. Assuming that each elderly is supported entirely by one working age adult, this means that the cost of old age support falls entirely on 11% of working age adults. In contrast, under a PAYG pension scheme that covers the cost of supporting the elderly through pension contributions by working-age adults, the financial burden is spread across all working age adults. In terms of figures in Table 15, the cost of supporting 11 elderly instead of confined to 11 is distributed across 100 working age adults. The general argument is that whereas under family support the cost of supporting the elderly falls entirely on a small minority of households, under a PAYG pension scheme the cost is distributed over a much larger number of households. This has two important implications.

First, the PAYG pension scheme offers a more stable financial support to the elderly than does family support. The explanation lies in reduced fluctuation due to a pooling of risks associated to spreading the cost of support over all working age adults instead of just those with elderly parents.

Second, related to the first, the PAYG pension scheme offers the possibility of ensuring that all elderly maintain at least the socially acceptable level of living standard. Generally speaking, family support of the elderly requires a social assistance scheme, such as the Five Guarantees scheme, to prevent poverty amongst the elderly. The implication is that a pension scheme would reduce the demand on social assistance schemes. Here it is important to point that poverty among the elderly provided the principal impetus for introducing of public pension schemes in the US and many European economies.

B. The MOCA/MOLSS Pension Schemes for Farmers: Success or Failure?

The piloting of formal rural pensions by the Ministry of Civil Affairs (MOCA) from 1991 was a bold undertaking unprecedented in developing countries. It has been contested ever since. In the late 1990s criticism by influential people at the centre became more serious, especially in the wake of the rectification in the insurance industry (see Chapter 2). This section aims to evaluate the pilot schemes in the light of the criticism raised and beyond. Are the schemes a failure and should be abandoned or have they it been a success story on which future pension policy can build?

Due to the critical development in the late 1990s, it has almost been forgotten that in 1995 a comprehensive evaluation of the pilot schemes by a group of highly qualified persons

had been undertaken. Before reporting the findings from our field visits, we therefore present the results of their research.⁹

1. The 1995 Rural Pension Evaluation

To reply to various criticisms and doubts about the rural pension schemes, MOCA decided at the end of 1994 to invite independent experts to conduct a comprehensive evaluation of the system, which was sponsored by Ing Insurance, a Dutch insurance company wanting to enter the PRC life insurance market. The review team was composed of eight experts and scholars from sociology, economics, demography, social security, insurance, and finance from several well-known teaching and research institutions in the PRC. It was chaired by Dr. Wang Sibin, then Head for the Department of Sociology at the Peking University. The team held the first meeting in March 1995 and completed the review at the end of that year. They attended to several basic questions

a. Was the Time Ripe for Introducing Pensions?

The Review Team (1995) agreed that with rapid ageing, economic development, and emigration in rural areas, the capacity of family support to old age would be further weakened. In addition, with the dissolution of the former collective security system in the rural sector since the end of 1970s, there should be an alternative to the community support to older people. Under such changing conditions, it is reasonable to expect that farmers should be looking forward to some formal arrangements to supplement the existing old-age support system. The questionnaire surveys confirmed the conclusion. Around 80% of farmers chose old-age problem as the top priority area for action, compared with other four areas including health care, poverty insurance, life insurance, and agricultural product insurance, regardless of their age, gender, and occupation. More than one third of interviewees cherished no illusions for family old-age support; on the other hand, the majority (more than 80%) of them believed self-support would be increasingly reliable with fewer children. Therefore, the team argued that it was fully justified for the Government to make some institutional arrangements.

The questionnaire surveys (Wang 1995) confirmed that two major reasons for farmers to participate in the pension schemes were whether or not they could afford the contributions and they believed they could be better off under the schemes, compared with bank deposits. And, at the same time, the surveys found that most rural households spent a lot of money on nonlife necessities such as presents to relatives at marriage and funeral ceremonies, cigarettes, and alcoholic drinks. Some spending thus could be diverted to a formal arrangement for old age such as the basic plan designed by MOCA, which offered a choice 10 contribution levels starting from 2 yuan every month. Such a low level of contribution was supposed to help raise the consciousness of farmers in supporting themselves.

Apart from economic reasons, those not participating in the scheme had worries about the policy stability and reliability. Some of them could still recall the broken promise made by the Government in the 1950s when rural households were encouraged to become the shareholders of cooperatives in rural areas. To convince farmers that the pension plan would be not only good value for their money but also reliable, it would be very helpful if the cadres at the grass roots could calculate comparative benefits in detail and set examples for the masses, besides ideological work. As Wang (1995) puts it, the ordinary farmers believe that the community elites

⁹ For an early empirical analysis of the problem of the scheme see also Krieg/Schädler (1995).

usually never take those businesses deemed to lose. Therefore, a consolidated political power at the grassroots level would be necessary to translate the pension policy into practice.

The plan of MOCA was thus deemed adequate and realistic considering the above-mentioned economic and political conditions. As Chen, the MOCA vice minister, argued in 1992, the rural pension system could be carried out in many areas with developed economy and effective political bases at the grass roots.

b. The Effects of the Pension Policy

As a team member (Zhang 1995) summarized, the pension policy had a positive influence on population control, local social stability, and economic development.

First, since introducing pension schemes in 1991, 7,600 couples had returned the quota in Yantai Municipality alone by the middle of 1995, which was allocated to them to legally have a second baby after a certain waiting period following the first baby girl. It could be a rational choice for farmers to seek old-age support through participation in the pension plan rather than having another baby. It would cost a minimum of 20,000 yuan to raise a child, while one third of the sum could be sufficient to buy a pension to secure a basic living standard.

Second, rural cadres and primary school teachers could sometimes get some old-age allowances when retiring, depending on the resources available and the capacity of the village committee to collect extra charges from farmers, which often created dissatisfaction among the mass as well as among retired elites. Nowadays, the village committee could use partial collective funds to subsidize the contributions of those elites. Then, in principle, those elites would rely on the MOCA pension plan, which emphasizes individual contributions to sort out their old-age support; thus, it was no longer necessary to levy extra charges on farmers when they retired. By contrast, some commercial insurance companies persuaded village cadres to use collective funds to pay for their life insurance policies without any individual contributions. The embezzlement of collective funds had almost caused the mass to burn the houses of those cadres. Therefore, the MOCA pension plan could help stabilize the army of local elites and could improve the relations between them and the masses.

Third, some older farmers think the MOCA pension plan could help improve the relations between them and their children. When realizing it may not be sufficient for old-age support, some older persons in Shandong would like to argue that it should be enough to buy some sweets or pencils for their grandchildren. In so doing, the pensioners wish to please the parents of those grandchildren so that they might not think "the older guys could only take without any giving."

Finally, as Zhang (1995) argued, huge accumulated pension funds eased localities' shortage in financial capitals, thereby promoting local economic development.

c. Coverage of TVE Employees?

It has been debated whether to cover the increasing TVE employees under the urban or rural systems. The team (MOCA 1995) agreed with the MOCA to set up a unified plan for both TVE employees and ordinary farmers. Several reasons for this were given.

- The operation of many TVEs is not stable, neither are the earnings of their employees.

- TVEs are usually sponsored by local resources, which thus have the liability to help other sectors of the communities.
- The majority of the TVE employees are farmers, who used to have no access to any social benefits. It is hard to imagine either to expand rather generous urban welfare benefits to this part of rural population very soon or to differentiate TVE employees from urban employees under a single system.
- The urban pension system has been struggling for survival.

d. Summary Assessment and Policy Recommendations by the 1995 Evaluation Group

All in all, the 1995 evaluation group gave a positive rating of the schemes. They argued that it is necessary to develop a formal arrangement in the rural sector to supplement the family support and individual efforts in old age, and that the MOCA plan would be workable in localities with developed economy and solid administrative bases at the grass roots. Moreover, it seems to them that the MOCA schemes, with great efforts of civil affairs authorities at various levels, have made some positive contributions to population control, social stability, and economic development in the pilot areas.

But the review team also expressed concern over the liberalized MOCA directives (Table 5), the actuarial estimates of the pension benefits, and the efficiency and the supervision of pension fund management. But they thought that these problems could be tackled on the basis of the MOCA concept. To this end they drew up policy recommendations for consolidating the pension plan.

First, pension benefits should be computed on an actuarial basis with realistic assumptions about life span and return rates so that the rural pension plan is self-balanced or fully funded. In other words, it should not follow the urban program that relies on state subsidies.

Second, the openness and transparency in the operation of rural pensions should be promoted to contain any departmental and individual interests, thus increasing the trust of participants. Besides the general supervision of MOCA, accountant agents and participant representatives should be appointed to oversee the implementation of pension plans at the county level, and to contain departmental and individual interests involved.

Third, the regulations on the investment of pension funds should be liberalized gradually and cautiously. According to the MOCA plan, the pension funds can only be invested in bank deposits and government bonds. Actually, some localities have invested the funds in other areas.

Fourth, some components of the pension program could be gradually commercialized. There are many segments in the process from the collecting contributions through investing pension funds till the delivering annuities. For example, a competitive market should be more effective than local authorities in fund investment and annuity provision.

Last, such a pure pension plan could be transformed into a comprehensive social security program. The participants should be able to use of accumulated funds in his/her personal accounts or even those in his/her family members for other purposes such as health care, education, and even productive investment in that health care is another major concern to

farmers and it is very difficult and expensive for farmers to borrow money from commercial banks.

2. Evaluation Based on Field Visits

The Department responsible in MOLSS could look back on a fairly successful past decade from two points of view. First, more than 80 million farmers, or about 16% of the total rural working population (NBS 2000) participated in the schemes. Second, an administrative network at six levels was set up, which employed more than 22,000 formal staff members.

In our interviews at the central level, however, we met with popular criticisms of the former MOCA (now mostly MOLSS) schemes. The key points were the following.

- Farmers were forced to participate in the schemes.
- Misuse of pension funds was widespread.
- The day-to-day administration is not reliable.

The rest of this section examines the operation of the pension schemes in the selected counties in light of these and other concerns. We pose the following questions.

- Is the participation compulsory or voluntary?
- Is the coverage universal or selective?
- Is the policy goal sensible?
- Is the administration and fund management reliable and efficient?
- Are the pensions actuarially estimated?

a. Compulsory or Voluntary?

How did local government go about spreading the scheme among the farmers? It was a joint effort by a number of committed administrators on a massive scale. The measures taken included the following.

- *Guidance by local governments.* First, it was very common for local authorities in the counties chosen to launch a large-scale education campaign for the rural pension schemes at the very beginning. Now we can still see the slogans concerning the rural pension schemes on the walls along the major traffic lines of the selected areas. No wonder, an 84-year-old Miao woman in a mountainous village heard of the rural pension scheme from her neighbors. Moreover, local governments at various levels issued documents and allocated tasks to lower levels.
- *The examples set by party members and cadres at the grass roots.* Following the instructions from the above, those community elites had to take the lead in making contributions for themselves or their children to the rural pension schemes. For example, a vice governor of Jiuchang township government made contributions for his grandchildren.
- *Collective subsidies to individual contributions.* A poor peasant we interviewed in Wuding County participated in the scheme in 1995 because he did not want to lose the conditional collective subsidies from the natural village. In Muping District, 18% of participants were subsidized by the collectives.

However, some special groups were urged or induced, if not forced, to take up the rural pension schemes. There are two types of cases that have to be judged differently.

- Besides cadres and party members at the grass roots, rural servicemen, rural teachers with agricultural *hukou*, and TVE employees are the target groups of the rural pension schemes in Wuding and Huangpi. In addition, the latter county also targets both-daughter parents. Although the participation of those group is, in a way, compulsory, the individual participants usually got some subsidies from the collectives or the local governments. Therefore, such compulsory measures should not have caused a strong aversion to the schemes.
- Things are different for the persuaded or even forced participation for other groups such as newly married couples and rural households involved in industrial and commercial activities (written material from a poor county in Anhui Province, 20/04/01). Most probably, they cannot get any subsidies for their participation in the rural pension schemes.

Then how widely and how often did such compulsion occur? The official responsible in Yantai Municipality told us that it happened in some areas of Yantai at the very beginning of the schemes, but it was stopped immediately by the municipal level. The official responsible in Yunnan Province suggested that the forced participation might be rather common in some inner provinces, but it was quite rare in Yunnan, which, as a border province, put social stability at the very top of the government agenda. Therefore, the Government never attempted to force certain groups to participate in the rural pensions, which could cause social dissent. Still, the governments at various levels worked very hard to campaign for the pension schemes.

b. Universal or Selective?

As discussed in Chapter 2, a major argument of MOCA against the commercial providers was that they were only targeting the cream of society and that some community elites could use the collective money to buy pension products for themselves. Such behavior, according to a MOCA Minister (Chen 1992a, b), created social dissent among ordinary people. Did the advocates of the pension schemes in the counties chosen try to cover as many people as possible?

Table 18 shows that the participation rates in both Zhaoyuan and Muping are quite high, while those in Wuding and Huangpi are rather low. In fact, the pension schemes in the latter two counties are targeting the cream of rural society. These differences reflect their economic conditions though this is not necessarily the case: More advanced Zhaoyuan should have done better than Muping, and Huangpi better than Wuding in expanding the coverage of their pension schemes.

It takes time for ordinary farmers to accept new things such as the pension schemes. To start with special groups, who are richer and better educated, may be justified. However, it is hard to understand why the pension scheme in Huangpi has still been targeting the few groups in the past nine years. Indeed, as we were told, it would be rather difficult to collect money from ordinary farmers, especially since they do not get subsidies (Chapter 6.C). That was a major reason for the agency responsible to shift its strategy from serving the whole working population to targeting the few groups in 1993. On the other hand, it is not impossible to expand the coverage to wider population in terms of the historical experience in Muping.

Table 18: The Operation of the Pension Schemes in the Selected Counties (2000)

County	Well-Off Counties		Poor County	Middle County
	<i>Zhaoyuan City, Yantai Municipality, Shandong</i>	<i>Muping District, Yantai Municipality, Shandong</i>	<i>Wuding County, Chuxiong Autonomous Prefecture, Yunnan</i>	<i>Huangpi District, Wuhan Municipality, Hubei</i>
Start of scheme	1991	1991	1995	1992
Administrative Staff (persons)	47 (county level 26, towns 21)	36 (county 15, towns and townships 21)	18 (county 5, town and townships 13)	22 (county 7, towns and townships 15)
Participants (1,000 persons)	116.0	149.3	12.8	10.3
Participation Rate (%)	68 (record level 87)	78	8.2	2.0
Payment of Contributions	Annually; some once a life-time	Annually; some once in a lifetime	Once a lifetime	Shift in 1992 from annual to once in a lifetime
Pensioners (persons)	1,497	11,531	66	228
Average Benefit (yuan/year)	691.4	88.8	30.3	1316
Total Accumulated funds (million yuan)	93.18	86.8	4.91	17.0

Source: Group interviews with the related government bureaus in the counties chosen.

c. Do the Schemes Provide Security in Old Age?

The intended objective of the former MOCA scheme was to combine with family support to guarantee a basic living standard of older people. In practice, however, they were not concerned too much about any low contribution rates of participants. They defended their policy design on the basis of the Singapore experience, which was supposed to start the old-age saving plan from a very low standard. At the very beginning of the scheme, it is absolutely necessary to have participants accept it rather than attempt to achieve a high standard.

Even now the official responsible in MOLSS still argues for this policy goal. The rural pension scheme is compared with the provident fund for housing. Nowadays every urban employee in the PRC has to put 5% of his/her salary into his/her personal accounts. Obviously, nobody can expect to use such little savings to pay for a mortgage of their accommodation. However, it has made a lot of difference meeting the growing demands for accommodations.

Our field visits have demonstrated that the pension schemes have indeed made some difference for the current pensioners in the following aspects. Then what difference have the pension schemes in the counties chosen made?

- From Table 18 we can see that the average pensions in both Zhaoyuan and Huangpi are higher than the defined minimum living standards for local farmers. In Zhaoyuan City, the contributions and the collective subsidies in many villages such as the Qianliuxing were based starting ages. The older the villagers, the higher their contributions and subsidies. In

doing this, many older participants in their fifties could receive decent pensions. In Huangpi, the focus groups made large amount of lump sum contributions to the pension schemes and thus are also qualified for a relatively high standard of pension after a few years of accumulation. The average lump sum contribution was 5,000 yuan.

- Due to the universal approach to pension development in Muping, the average pension in 2000 was only 88.8 yuan. However, looking at Table 19, we can see that more than 15% of pensioners have received more than 100 yuan of annual benefits. According to the official responsible for rural pensions in Muping, the cash a parent can normally get from each son is a little more than 100 yuan per year. In some sense, thus, the rural pension scheme is the same as another son for most older people.

Table 19: Current Pensioners in Muping in 2000 by Benefit Rate

<i>Annual benefit (yuan)</i>	<i>Pensioners (persons)</i>
Less than 100	9,774
101-300	1,501
301-500	81
501-1,000	35
1,001-2,000	125
2,001-3,000	6
3,001-4,000	4
4,001-5,000	3
5,001-7,000	0
7,001-8,000	1
8,001-20,255	0
20,256	1 ^a
Total	11,531

^a A former branch secretary to a CCP village committee who obtained a huge subsidy in his 50s. Source: Interviews with Muping Labour and Social Security Bureau (May 2001).

- For a pensioner in Guanqianjiangjia Village of Zhaoyuan City, the pension benefit he receives quarterly is the most certain and regular as well as the biggest income, although he is still working in TVE and a little piece of land. By contrast, the wage incomes from the TVEs are distributed annually (Chapter 6.C).
- Finally, we can recall a photograph of a smiling old woman in Zhaoyuan, which was taken when she was receiving her benefit. The big smile on her weather-beaten face seemed to come from the bottom of her heart. In addition, a young woman we interviewed in Guanqianjiangjia Village also looks forward to her retirement pension in the far future. She is working as an accountant in a TVE and, meanwhile, is looking forward to similar benefits as her urban counterparts.

d. Is Administration and Fund Management Safe and Efficient?

We are told there are no cases of misusing rural pension funds in the selected counties, although there are some stories about other areas. We have no reliable source to confirm this, let alone to tell how widespread such problems are. Some suggest that the cases found were just the tip of the iceberg; others maintain that the problems are neither so serious as some people imagined nor more serious than with other funds.

In Zhaoyuan and Muping we found reasonable evidence of a sound administration. Compared with developed pension schemes in Western societies, the PRC rural pilot schemes

are small and based on simple regulations as regards contributions and benefits. They are also less complex than the urban scheme. However, within that framework the administration of the scheme has reached a degree of professionalization from which an extended and more complex scheme could start. The scheme is run based on a well-regulated formal organization, with comprehensive records on its operation. The basic administrative procedure is standardized nationwide, following regulations of the Ministry of Civil Affairs. The staff has a considerable degree of expert training and can be considered as social professionals. Recent information technology is used to handle large sets of data.

The administrative structure in the counties we visited is similar. The details for Zhaoyuan, Yantai (Shandong) are as follows. There are 47 full-time staff at the county and town levels. Of these, 42 have a university or polytechnical certificate, and 23 have a professional certificate.

All relevant insurance data are fully recorded, on three levels.

- There is a computer file with data on each participant, including state ID, birth date, start of participation, total contributions, collective subsidy, individual contributions, code number. The software was supplied by the Ministry of Civil Affairs.
- The same data are also kept in written form, in books at the county level (in Muping, at the town level)
- The participants, the farmers, each have their own booklet on their insurance data. Each year administrative staff go to see the farmers to compare the data in their booklets with those in the centrally held records. According to the official in Yantai Municipality, the individual counties printed out the individual account statements every year over the past 10 years. Since this year is the tenth anniversary, they will provide more detailed information to individual participants.

Funds are invested by the county on a semiprofessional basis. The director himself is qualified in matters of investment. In Muping there are weekly professional meetings on investment. Up-to-date Internet charts on the development of government bonds are used. The person responsible in Zhaoyuan is proud of Zhaoyuan's investment performance over the past 10 years. He showed the most recent success in an on-line transaction of state bonds. The return rate of this transaction was 5% in four-month time. So they earned 11.9 million yuan extra return above the interest promised to farmers (which is determined by the central authority for rural pensions according to interest rates of bank deposits). It has been a little higher than the current interest rates of bank deposits. Thanks to the good performance in the pension fund investment, according to regulations, part of the extra returns can be used to subsidize the administrative costs. It would be far from sufficient if only the administrative fees drawn from the current contributions, equivalent to 3% of the contributions of each year, could be used.

Benefits are paid to bank accounts. Every participant has a free bank account and can even use a money machine. In poorer and mountainous areas like Yunnan, this may be different.

There is a special social security agency which, in Muping, is part of the labor and social security bureau. It has five sections: internal, finance, auditing, fund management, and general office. There is intensive training of staff, for example in Yunnan Province there is a compulsory training three times a year that is much wanted by the officials. Some of the leading officials we interviewed were enthusiastic about their work. They showed a specific social motivation beyond bureaucratic observance of formal rules. They were strongly committed to the course of

providing old-age security although no personal gain ensues from this activity, unlike those local politicians and administrators who have become managers of commercial companies ("community capitalists," Chapter 6.A).

Thanks to their administration, the pension schemes in Yantai Municipality are still going smoothly in recent years despite an adverse political environment: While local governments no longer launch campaigns for rural pensions and the schemes were dogged by various rumors due to the ongoing rectification, the executive agency of rural pensions in Zhaoyuan can still collect 10 million yuan each year, and, at the same time, they are not afraid to give back money to those participants who are getting worried about the change in the government policy.

According to Zhaoyuan executive agency, they gave back about 2 million yuan each year to those farmers influenced by persistent rumors in recent years. As a result, Zhaoyuan can collect 8 million of new contributions. In addition, according to the Muping executive agency, 9,800 farmers have newly participated in the rural pension scheme.

In short, rural pensions became a routine job in the local government, and making contributions to the schemes became voluntary for many farmers, at least in Yantai. In fact, in Yunnan, rural pension schemes could have been gradually accepted by some farmers in many other localities:

In April 2000, an MOLSS official was sent to Yunnan to investigate and rectify the rural pension schemes. As a result of the MOLSS investigation in Yunnan in April 2000, the rural pension schemes are now being rectified, so the local executive agency does not go to the grassroots to collect contributions.

In poor areas, however, there remain problems and constraints with the practice of rural pensions, despite committed administration.

e. Is the Pension Formula an actuarial estimate?

This question concerns the central authority. According to the original design of MOCA, the annual return rates credited to personal accounts of individual participants before and after their pensionable ages would be fixed at 8.8%. In 1993, however, MOCA realized that a fixed return rate for more than 60 years could not be assumed.

Since 1994, therefore, although the annual return rates credited to individual accounts after the pensionable age is still fixed at 8.8%, the return rates before the pensionable age have been floating with the interest rates of bank deposits. The floating return rates over the past 10 years have been determined as follows: from 1991 to the end of 1993, the annual return rate was 8.5%; from the beginning of 1994 to the end of 1995, 12%; it was 12.5%, 8.8%, and 6.8% in 1996, 1997, and 1998, respectively; and since the beginning of 1999 it has been reduced to 2.5% annually.

There should be no difficulties for pension funds to achieve a little higher return rate than the interest rate of bank deposits. The big concern is whether the fixed return rate at 8.8% for annuity is realistic or not. In addition, it is also debatable whether other assumptions such as life expectancy are adequate. The annuity formula

$$\begin{aligned} & \text{Monthly annuity since 60 years old} \\ & = 0.008631526 \times (\text{total accumulated funds at age 60}) \end{aligned}$$

is actuarially designed only in a most basic way. One interviewee said that a Japanese life table was used. Interestingly, this formula is almost the same as the benefit formula for the urban individual account pension

$$\begin{aligned} & \text{Monthly annuity in the first retirement year} \\ & = (\text{total accumulated funds at retirement ages}) / 120. \end{aligned}$$

This seems to be a coincidence. The major difference between the two formulas is that the pensionable age under the rural pension scheme is fixed at 60 years compared with the changeable pensionable ages for urban pensions from ages 45 till 60, although the life expectancy in the urban sector is higher than in the rural sector. Moreover, the urban pensions will be adjusted for the rise in social average wages. By contrast, rural pensions would remain unchanged from pensionable age till death.

Special benefits are calculated on a semiactuarial base, for example when actuarial deductions from benefits are made in the case of early retirement. Similarly, when a TVE wanted its employees to join the scheme at a certain preferred benefit rate, the contributions needed to achieve those benefits were calculated.

A problem concerning the rural pension calculation is credibility and trust. Some localities wrote the expected benefit rates in the handbooks of individual participants according to the fixed annual return rate of 8.8% for the whole contribution period. This was done to increase the transparency of the schemes. Since the return rates for the accumulation period became floating in 1994, it has been very difficult for those agencies to urge participants to accept the decreasing return rates.

3. Summary Assessment of Pilot Schemes: A Reasonable Basis to Build on

We can now summarize the findings of the evaluation. There is little solid evidence that could support the far-reaching criticism brought against the scheme (Box 17). The system clearly has problems (Box 18) but it is difficult to see why they should be taken as a reason for abandoning it. If the scheme is not wanted for political reasons, this decision should not be justified by an alleged malfunctioning. All in all, the scheme has considerable achievements (Box 19).

Box 17: The Popular Criticism of the Rural Pension Schemes Needs Serious Qualification

1. *Forced participation of farmers:* This could be partly true in the early years of many pilot schemes, and could still be the case in some poor areas. But most farmers seem not only to enter the system voluntarily but some also feel free to retreat from it, especially in rich areas.
2. *Misuse of pension funds:* No evidence suggests that this problem is more serious in the rural pension schemes than in other, public or commercial, institutions in the PRC. Compared with the urban scheme where all accumulated funds have been lost, the rural funds are fairly well managed. Low misuse seems rather likely in well-managed areas like Yantai. In addition, some misuse of rural pension funds might recently have been triggered by the bleak prospects of the system and the ensuing low contributions from farmers. These problems are policy produced.
3. *Bad management:* The field visits suggest that the day-to-day administration in rich areas like Yantai is reliable, computer-aided administration is routine at the county level, and, moreover, the pension fund investment is also efficient.

Box 18: Problems of the MOCA Pilot Pension Schemes

1. *Participation:* Participation has been low in poor areas. Some places, including pioneering counties like Huangpi, have even formally targeted the cream of society. In addition, the participation rate is decreasing in rich areas in recent years due to the ongoing rectification and long-term nondecision.
2. *Outcomes:* Contributions and benefits are low not only in poor areas like Wuding but also for many participants in better-off areas. Contributions are sometimes made only once in a lifetime. These are embryonic "pensions." The scheme has neither defined benefits nor defined contributions. It is a form of organized saving rather than social insurance.
3. *Actuarial validity:* Compared with the individual accounts under the urban pension program, the benefit calculation under the rural pension schemes should not be a concern to the decision makers. However, it is obviously mistaken to fix the annual return rates in advance before the pensionable age. There are basic actuarial elements but they must be developed.
4. *Equity:* There are some equity problems with the current practice in some localities (Chapter 6.A).

Box 19: Achievements of the MOCA Pilot Pension Schemes

1. *Objectives and outcomes:* The original policy concept by MOCA is realistic with regard to the aim of enhancing old-age security in the countryside by pensions as part of a broader income mix. Even at the current low level, the benefits received by the pensioners make a difference for many of them.
2. *Institution building:* The schemes are not social insurance but rather an organized saving plan for farmers. Compared with other developing countries, this is an achievement.
3. *Administration:* A standard operational procedure has been established, but not only in well-off areas.
4. *Acceptance:* The pension schemes have been widely campaigned and have been accepted by many farmers.

A key conclusion is that the performance of individual pension schemes depends heavily on local economic conditions. Both the existing evaluation and our own case studies suggest that the MOCA/MOLSS pension program is workable for a significant part of the population in better-off areas. In addition, they would also have some positive impact on the socioeconomic development (Chapters 6.C and 6.D). Finally, many problems accompanying the rural pension development are politically induced, such as insufficient encouragement to participants and administrative staff, little coordination between government departments, and, above all, the current destabilization of the system by a protracted period of nondecision and uncertainty both for local administrators and participants.

C. The Modernization of Rural PRC—Toward Undivided Citizenship?

In this section we analyze recent changes in rural PRC—above all TVE, migration, public pensions, and village semigovernment—and their impact on the forms of social exclusion and inclusion. We then draw conclusions for political reform of old-age security.

Over the last two decades new social institutions have emerged in PRC's rural society: the household responsibility system, rural enterprises owned by TVEs, and grassroots democracy in the villages based on village committees and village meetings. They have transformed the social structure of rural PRC: the organization and distribution of work, income and wealth, the shape of social relationships, and the patterns of power and stratification. In this process new opportunities for many rural citizens have opened up, but at the same time new social divisions and exclusions have emerged.

The most recent institutional innovation is the introduction of public provision for old age, namely the piloting of pensions by MOCA since 1991, and, notably, the adoption of the older urban pension scheme in some rural enterprises. The new institution, public pensions, is closely linked to the others, especially to TVEs and villages. TVEs and villages are major pillars of its operations, and, vice versa, TVEs and villages use the public pension schemes for their own operations, as will be shown below.¹⁰ A new institutional structure has emerged, producing new inequalities and new forms of exclusion, but lacking new rules and direction.

- *Institutional structure:* A new, complex institutional arrangement of organizing rural old-age security—based on the interplay of public pension schemes, TVEs, and villages has emerged. But there is a vacuum of rules. Villages and TVEs organize pensions in a haphazard and nontransparent way.
- *Outcomes:* This structure produces new social divisions and inequalities. Pension schemes create divisions of entitlements. For villages and TVEs, public pensions are a new source of power and selective reward.

However, this is primarily a story of social inclusion: The ingrained social division between rural and urban society is breaking up. Through the new institutional structure, rural citizens increasingly share in opportunities hitherto reserved to urban citizens, in the economy, and now also in social security. But there is no new, comprehensive model of citizenship as yet.

¹⁰ For the wider context see the seminal analysis by Sarah Cook (1999, drawing on Gordon White) of 'welfare entrepreneurship' in the rural PRC.

1. The Impact of TVEs

Since the 1980s TVEs have been a major factor of rural economic growth and the PRC economy at large. It has gone largely unnoticed (Cook 1999) that in the 1990s TVEs have also become a major factor of old-age security in the rural PRC. This refers to public pensions, not to occupational pensions.

On the one hand, the proliferation of TVEs is challenging the pilot schemes for rural pensions: The underlying assumption that the pilot schemes address farmers (people working on land) has become invalid. Many people have become employees of factories and enterprises with little concern for the piece of land they still may have got.

On the other hand, the TVEs play an active role in operating pension schemes although this role has never formally been assigned to them. The impact of TVEs on old-age security is far-reaching though little noticed. A maze of legal and financial links between the enterprise sector and public social administration has emerged.

- The existence of a TVE is a major factor in determining whether a village joins the public pension scheme or not because contributions by the village are mostly financed out of profits from a village-run enterprise.
- The profit of a TVE may determine how much subsidies a village that has joined the scheme may pay to its participants.
- Some TVEs pay a direct subsidy to their employees to top up their contributions to the public pension scheme.
- Even the entry of the TVE workers may be collectively initiated and organized by the TVE. The contributions may also be collected by the enterprise and sent to the pension administration at the county level as a whole, as we found in a TVE where one of our interviewees worked as a cashier (Zhaoyuan County, Yantai Municipality).
- Pension subsidies may be a new instrument of corporate policy of the TVEs. High subsidies help recruit and secure more qualified workers. At the same time some TVEs are reluctant to pay subsidies.
- Even without subsidies TVE employees tend to have higher incomes than mere farmers and are thus in a position to pay higher contributions to pension schemes, both public and private.
- Working in a TVE with a long-term contract may feed people into the urban pension scheme.

The interplay of TVE and pensions has a profound impact on rural society. The first is social inclusion. TVEs contribute to the erosion of the rural-urban divide—not only by rural industrialization and urbanization, but also with regard to social security: they enable more people to join the rural pension scheme and some to join the urban scheme.

Since the mid-1990s the economic development of TVEs has been running into problems. New concepts and new directions are called for by external observers. But the role of the TVEs in old-age security equally needs revision. The way different groups are included in different pension schemes has grown wild and needs clarification (boxes 20 and 21). *Hukou* is less and less suited as a basis of organizing old-age security. But what should replace it?

**Box 20: Who Gets What Pension in Rural PRC?
The Erosion of the Distinction Between Rural and Urban**

Information by the Department of Labour and Social Security, Hubei Province

In Hubei as in most other provinces, a key strategy of rural economic development is the promotion of TVEs and related migration to towns and small cities. This form of urbanization aims to minimize migration to big cities. In the process the distinction between rural and urban is blurred. People may be employees with some employer while retaining a rural *hukou*. These people are neither fully rural in the old sense of farming nor are they fully urban like city dwellers. At the same time the division between rural and urban pensions is blurred. Rural persons may be eligible to urban pensions.

At present there is a confusion of who gets what. There are no clear criteria. There are three in-between groups.

- *Migrants to big cities* (floating population): If they have a contract of more than three months, they are, on paper, eligible to urban pensions. Some employers try to prevent them from joining to evade contributions. In that case the urban pension scheme loses young blood, receives less contributions.
- *SOE/COE employees in towns and small cities*: They should be included in the urban scheme though there is no clear policy as yet.
- *TVE employees*: They should in principle join the rural scheme but at the township level they often belong to the urban scheme. Some of the employees may even have an urban *hukou*. The enterprise may prefer urban pensions because they are considered more reliable and their financial viability is guaranteed by the Government. In Xiantou County (*shi*) the economy is dominated by TVEs, most of which let their workers join the urban scheme.

There is a tendency that the employment contract rather than the *hukou* determines who gets what pension. This would shift eligibility to social benefits from a legal to an economic criterion, mirroring a person's situation more realistically. At the moment there is confusion that calls for regulation.

Box 21: Mix of Rural and Urban Pensions within One TVE

A brick factory in Jiuchang Township, Wuding County, Yunnan

Wuding is a national poverty county. The factory was founded in 1992, initiated by the county government. There are 60–70 workers, most of whom come from up to 80 kilometers away but sleep in the factory premises. About 14–16 workers are from the local township. Two managers are locals while two others are from the mining company at the county level that runs the factory.

There is a peculiar pattern of selective reward.

- The local managers participate in the rural pension scheme and get no subsidy from their TVE (only from their village), while the county managers participate in the urban scheme, enjoying a generous annual subsidy of more than 1,000 yuan (own contribution: 100 yuan).
- By contrast, local and migrant workers are treated alike. Like the local managers, they get no TVE subsidy for their pension. The TVE is economically too weak to pay subsidies.

How widespread are TVE-based pensions? For 1993/94 Taubmann and Heberer (1998), in a study of 38 enterprises with 2,112 workers, found that 8% of the enterprises introduced pensions and less than 2% of the workers participated in the scheme. Since the public scheme was being phased in during these years, we may assume that coverage has increased considerably since. In areas like Yantai Municipality, with a coverage of more than two thirds of the rural population and thriving TVEs, a much higher proportion of participants from TVEs is likely.

Taubmann and Heberer (1998) also found that only 117 workers (5.5%) passed on their land (unofficially) to somebody else, mostly to family members, kin, or other farmers of the village. This suggests that land was considered as a safety net of last resort. Still, the living conditions of these persons are largely shaped by their TVE employment. We may assume that the number of people who pass on their land has increased in recent years.

Pension entitlements are not only a benefit to the entitled; they may also benefit the TVEs in economic terms. This explains much of their prevalence. Pensions have three functions for a TVE:

- attracting qualified personnel by offering subsidies for pension contribution, either under the rural scheme or requiring higher and legally defined rates of subsidies/contributions under the urban scheme (Box 22).
- controlling the workforce by offering pension subsidies to some while denying them to others; this is one example of selective rewards that are common in enterprises all over the world; and
- the new rural elites, the “community capitalists” (Wank 1993, 1999; cf. Taubmann/Heberer 1998) and company managers who emerged in the 1980s, may use pensions as another way of enriching themselves, by arranging for high company subsidies to their own pension account.

Box 22: The Economic Use of Social Security

TVEs in Zhangxin Town, Zhaoyuan City, Yantai Municipality, Shandong

In this well-off area, there are many profitable TVEs that are in a position to provide generous subsidies for their employees to join the rural public pension scheme. As reported by the town government, pensions are seen as an instrument to attract qualified workers and to stabilize the workforce. In most TVEs all employees are included.

Normally TVEs take a much higher share of the pension contributions than the participants themselves. A subsidy would amount to 40–50 % of basic wage, which is about 10–12% of the total actual wage. The employee pays only 2% of the basic wage, i.e., less than 1% of the total actual wage. The enterprise actively contacted the pension administration at the county level to design a scheme suited to its needs. The enterprise decided about a desired pension level and the county labor office calculated the contributions required to reach that level.

This arrangement is evidence of the pronounced interest of the enterprise in using pensions as a means of securing labor supply. Both sides, employers and employees, profit from this solution. However, employees of other enterprises that cannot or do not want to run such a scheme lose out. The enterprise uses the public rural scheme as a kind of occupational pension.

The last two points—selective rewards for the workforce, local elite privilege—lead to the new patterns of inequality and social exclusion attendant to the TVE-pensions interplay. Inequalities emerge in several dimensions:

- villages with TVEs versus those without or with weak TVEs,
- poor areas with few TVEs versus richer areas with many,
- locals versus migrants,
- members of local elites versus ordinary citizens, and
- men versus women.

In this way, the introduction of pensions reinforces the inequalities of wealth and earnings ensuring from the rise of rural industry (for these inequalities see McKinley/Brenner 1999). Boxes 23–25 illustrate these divisions. In the case of elite and gender divisions, the impact of TVEs mixes with the impact of the village organization; these divisions will therefore be treated in the context of village (see below).

Box 23: TVEs Make a Difference—Pension Winners and Losers

TVEs in the Special Economic Zone in Zhaoyuan City, Yantai Municipality

There are eight villages in the zone, six of which joined the public rural pension scheme (with all their citizens, altogether 3900 participants over the last eight years). Two villages did not join because their TVEs were underdeveloped and could not afford subsidies. The six villages pay a subsidizes 50% of the total contribution. Those who retired get an equivalent of 300–500 yuan per year on top of their pensions. The money is taken from the collective economy, mainly the TVEs.

Box 24: Areas with Underdeveloped TVEs—A constraint on Pension Development

Yunnan Province

In Yunnan, less than 5% of the rural workforce belong to a TVE. This is a major reason for the low participation in the public pension scheme. There is less money income (more production for subsistence from land), incomes are lower, and subsidies to pension contributions by employers less likely. The problems of setting up a TVE and achieving a reasonable profit are manifold.

- Enterprises may have to close down during harvest season to allow the employees to cultivate their land. In TVEs with low wages, rural citizens have to rely more on a mix of farming and factory employment rather than give full priority to employment. In these cases the harvest season becomes more of a problem.
- Small-scale TVEs run by a group of households are more common than in other provinces.
- TVEs tend to use low-tech equipment and rely on raw materials. Enterprise activity often revolves around agriculture.
- Cost of transport are high because Yunnan is mountainous.

A 35-year-old farmer from the remote, extremely poor village Huapo, Wuding County, is eager to join a nearby TVE, a lead mine, but the neighboring village admits only three persons from his village, and he thinks he is not smart enough. In this case the limited number of jobs in an economically weak area combines with local protectionism. The man once left the village for a job in another place but was cheated by the employer and received no wage, so he left after 10 days. Withholding due wages is not uncommon in the unregulated PRC labor market. The man, therefore, gave up the idea of migrating to a town or city to improve his income.

Another 35-year-old farmer from the same village rejects the idea of going to the TVE because he deems the work extremely hard and badly paid 20 yuan per day, even less if the work is not satisfactory). Moreover, he could not leave his land for a long time.

Box 25: TVE-Based Public Pensions—A Source of Social Divisions

A sweets factory owned by Dongliang Village in Zhaoyuan City, Yantai Municipality, Shandong

The factory was set up in 1980, with 80 workers (now 200). It is operated by a company group owned by the village. All companies of the group pay subsidies to participants of the public pension scheme. Half of the workforce are villagers, the other half are migrants from the neighboring village.

In 1992, right from the start of the public pension scheme in that area, the factory organized a collective entry of their workers to the scheme. Each worker receives a subsidy of 200 yuan per year from the employer. The subsidies can only be paid because the factory is profitable. As one of the managers said this may change with the economic situation.

The migrant workers get no subsidies even though they come from the neighboring village and go home every night. This confirms the findings of the study by Taubmann and Heberer (1998) who analyzed 38 enterprises with 2,112 workers, including 276 migrants without change of household registration (data collected in 1993/94). Discounting free accommodation in the factory premises, almost half of these migrants did not get any kind of social benefit from the employer, as compared with 30% of the local village workers. The study also found that temporary workers even do worse, with 56% receiving no benefits. The two disadvantaged groups may overlap, although, as in the sweets factory reported here, they need not coincide. While the discrimination of temporary workers with regard to social benefits could be justified, the discrimination of migrants with longer employment cannot. Temporary workers seem to be the losers of rural development (McKinley/Brenner 1999).

Some workers, apparently those with high wages (up to 10,000 yuan per year) and a long employment record (working in the factory since the early 1980s), are privileged: They build up entitlements to two pensions, one from the enterprise, and the other from their village.

Both forms of discrimination are a form of local protectionism: locals versus migrants in the first case and people involved in local networks versus those who are not.

2. The Impact of the Village Organization

Like TVEs, villages influence the position of participants in the pension scheme in many ways. Different criteria of distribution are applied in the process. First of all, the ability of villages to pay subsidies to villagers depends much on their collective revenue, mainly on their TVE. Those citizens who happen to live in a village without TVE or with one that makes little profit lose out.

Moreover, subsidies are mostly proportional to the size of the contribution made by the participant him/herself. This may seem reasonable. On closer examination, however, this turns out to be kind of regressive redistribution from poor to rich: better-off people get a higher subsidy from village funds than the less well off (Box 26). In this way, the village subsidy reinforces inequality. Although paid under a public pension scheme, the "subsidy" is no subsidy in the traditional sense to support the poor, such as minimum pensions that add a floor to an earnings-related scheme. At the face of it, it looks more like the employer's share in pension contribution that is common in Western countries: Employer and employee each pay half of the contributions. However, in Western countries the employer's share is seen as an implicit part of the employee's wage whereas the village is not an employer of the villagers. The subsidy is not determined as part of a price in the labor market (like the employer's share) but by the power of local elites, in the case described in the box by managers, who sustain a system that profits them.

Box 26: Village Subsidies to Pensions—Elite Privilege and Regressive Redistribution

Qianliuxing Village, in downtown Zhaoyuan City, Yantai Municipality, Shandong

A village electrician with a low wage (400 yuan per month) and land can afford 18 yuan as annual contribution to the public pension scheme. As a subsidy the village adds the same amount. A man who works as a manager in an enterprise and belongs to the same village pays 140 yuan annual contribution and gets additional 140 yuan as subsidy from the village.

Other strategies by villages include the closure of the local labor market. We have described the case of a farmer in a poor village who was excluded from the TVE of a neighboring village because the TVE admitted only three nonlocals (Box 24). Another strategy is to pay TVE subsidies only to workers from the village who owns the TVE (Box 25).

What criteria are used by villages for the unequal treatment of their citizens? There are three different grounds of welfare entitlements: achievement, merit, and need (Chapter 3.C). Public pensions are primarily achievement-based since a contributor pays into his/her individual account, from which pensions will be paid. Subsidies change the picture. Apart from proportional subsidies just described, subsidies are often based on merit. People are rewarded not for achievements in the market or because they are needy but for a special contribution to the community or the nation at large. In addition, a gender distinction comes in (Box 28). Women tend to be discriminated under the pension scheme. Often discriminations in the labor market or in a TVE and in social security reinforce each other (Box 27).

Box 27: Merit and Gender as Bases of Pension Entitlements

Huangpi District, Wuhan Municipality, Hubei

Huangpi is the largest and most populous county in the municipality, economically slightly below average, and predominantly rural.

Wuhan Municipality was a pioneer of the MOCA pension scheme. In 1992 all counties started to set up the scheme. During 1996–1998 it became a prime government target at the township level. Eligibility to the scheme and subsidies paid by the village are defined by criteria of merit. The following groups are targeted as eligible.

- Village cadres
- TVE cadres and employees
- Two-daughter families
- Servicemen
- Farmers
- Rural primary teachers

In 1992/1993 contributions were paid annually. When this turned out to be too complicated, a system of lump sum (once-in-a-lifetime) payment was adopted, with contributions ranging from 1,000 yuan to 8,000 yuan. Cadres received the highest subsidies (2,000 yuan, shared by village and town) to top up their own contribution of 1,000 yuan while other merit groups received less, depending on the village, e.g., 500–800 yuan for two-daughter families. Farmers (unless belonging to the latter group) get no subsidies. Wives also generally get no subsidies.

Two criteria are apparent: merit and gender.

Merit is defined in political, economic, and social terms: Cadres, TVE members, teachers, and two-daughter families are privileged, whereas farmers are excluded from subsidies. In many provinces in the early years of the scheme the cadres took the lead in joining (driven by incentives and/or soft coercion) to induce ordinary farmers also to join. Their merit is to carry out governmental tasks. In addition their salary is low. Rural primary teachers are not paid by the state but by the village.

The privilege of two-daughter families is noteworthy since under pension schemes and allowances run by the State Family Planning Commission one-child families are also targeted. In Huangpi, by contrast, the merit of following the family planning policy comes second to the criterion of need (not merit), namely that in these families there is no male breadwinner to support the parents in old age.

The discrimination of farmers (who are the majority of participants all the same) seems to account for the extremely low coverage of the pension scheme in the county, which is not much more than 1% of the rural population.

Gender: The denial of subsidies to wives seems to be the main reason why 69% of the participants in the scheme are male. Other reasons may reside in gender relations within the households, namely a dominating role of the husband coupled with the notion that only one partner should join. Before, a wife may indirectly share her husband's pension but when he dies 10 years after pensionable age, the wife receives no money from the scheme.

Box 28: Discrimination of Women

A female TVE worker in Jiuchang Township, Wuding County, Yunnan

She is married, with two children aged 4 and 7, and earns 2,000 to 3,000 yuan per year in a brick TVE. Her husband also works there as a group leader at a wage of 5,000 to 6,000 yuan per year. He has a small pension entitlement from a once-in-a-lifetime contribution of 250 yuan supplemented, by a 50 yuan subsidy by the village.

In one aspect she is not discriminated: She has not been left behind to work on the land in their village although in the whole of Yunnan, women account only for 18% of TVE employees (National Agricultural Survey Office 2000). But her wage is well below her husband's wage. He explains this by saying that the work in a brick factory is too heavy for women and that their output, therefore, is limited. However, he works as a group leader, which implies less physical work.

Unlike her husband, she is not entitled to a pension. The village subsidy was only paid for one of the spouses. It was he who attended the meeting of the village committee where the pension scheme was introduced and he put his name on the list.

We may conclude that gender discrimination could be avoided in a more formal social insurance scheme that legally provides benefits for both men and women and that standardizes the procedures for individuals to join the scheme.

Although criteria of merit—like teaching village children—may appear reasonable, there is scope for people to define who has merit and who has not. Merit is not a natural property but defined by people who have the power of definition. The example from Huangpi county shows that this definition can be very special. Local elites may use this instrument for patronage and discrimination.

In the PRC, the village is more than an administrative unit. It is also a community based on mutual aid and solidarity. This may include rewarding those members who have served the community (Box 29). But again local elites decide who gets what awards.

All in all, a three-dimensional picture of social exclusion in the rural PRC emerges (Figure 4).

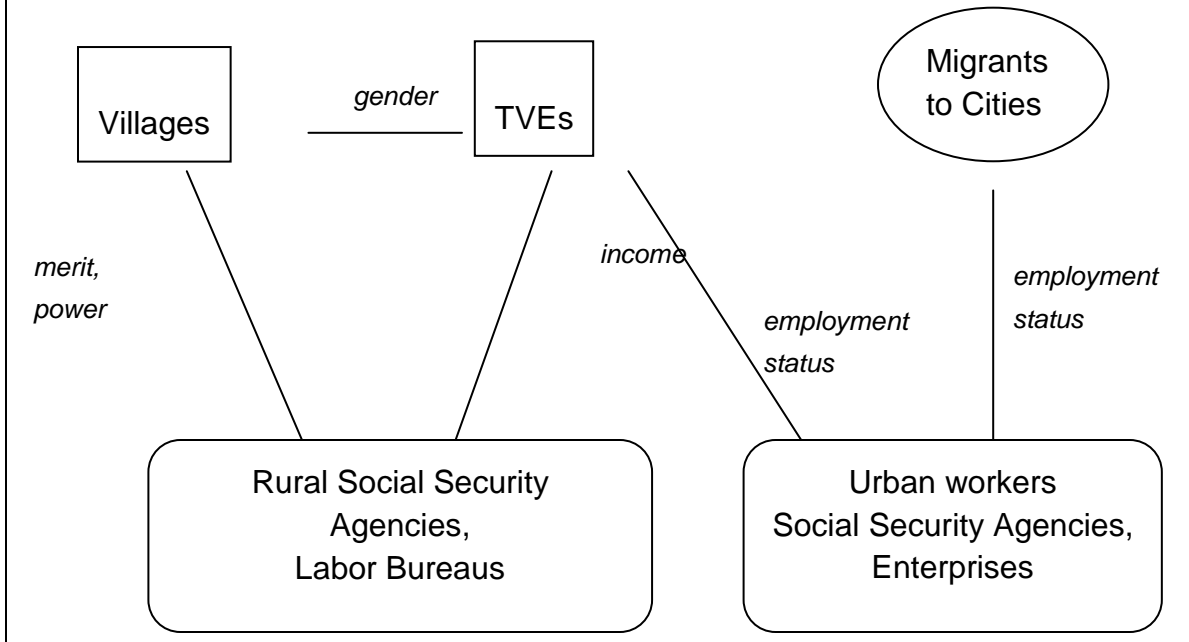
Box 29: Community as Basis of Pensions Entitlements

Guanqianjiangjia Village, in an agricultural setting in Zhaoyuan City, Yantai Municipality, Shandong

The village has 240 households (780 people) with an average annual income of 4,600 yuan. There are 114 elderly including 26 pensioners. 350 people qualify for the pension scheme, 330 actually joined.

When the scheme was introduced in 1991, retrospective contributions were made for the years 1984–1991. The village paid 3,000–10,000 yuan to each participant, depending on his/her work for the village, in the village's TVE and in public works.

Figure 4: Old-Age Security in Rural Areas—Dimensions of Social Exclusion



3. Women's Discrimination: A Reason for Social Security Reform

Women's discrimination has figured in several exemplary cases described in this section and in Chapter 6.A on family and land. Discriminations extend to many areas, often reinforcing each other.

In many countries, women are discriminated in the PRC's labor market. In 1996, only 35% of TVE employees are female (National Agricultural Survey Office 2000). Type of ownership—town, village, union of household, household—makes no big difference. Men dominate not only in those jobs traditionally considered as male, like construction (10.5% female workers) but also in more "female" sectors like trade and catering (45% women, which is the maximum of all sectors). In Shandong and Hubei the proportion of women in TVEs is slightly below average, in Yunnan it is far below, at 18%, but rising. Furthermore, if women are employed in TVEs their wage tends to be lower. As shown above, nonparticipation or low wage in a TVE entails lower participation in the pension scheme.

The pension scheme as run by the villages also tends to disadvantage women. Often only the husbands join the scheme or the village pays no subsidies to wives. If the husband dies earlier than 10 years after reaching pensionable age, the widow will be paid the remaining sum, though. This is a kind of derived survivors pension.

In the family it is the women who often carry the burden of supporting parents and suffering attendant conflicts (Chapter 6.A). As regards land, women are often left behind when the men go to work in a TVE or migrate to cities. Women migrate less.

Participation in commercial schemes is affected by lower income just as public schemes. Moreover, under commercial insurance women have to pay a higher premium because they have a higher life expectancy. Talking to local insurance agents we rarely came across unisex tariffs common in some Western countries and, for example in Germany, even enforced by law in some areas.

We can conclude that under the traditional sources of providing for old age—family support and land—and under the more recent public scheme, women fare badly. When praising the traditional sources it should be remembered that "family support" and "land" mean (not only but predominantly and increasingly) women's work and burden. These are the social cost of relying on the old way. Under public schemes, more can be done for women if so desired (Box 30).

Box 30: Reducing Discrimination of Women in Old-Age Security

In the field of old-age security, introducing elements of social insurance would reduce the discrimination of women. These might include

- extending public schemes to reduce the reliance of the elderly on family support and land, which tend to be a bigger burden on women than on men;
- establishing a right to participate in old-age pensions for both sexes rather than leaving it to villages to decide who may join and who is entitled to subsidies;
- making participation compulsory would prevent husbands and villages from trying to make women renounce their rights;
- formalized procedures of joining and claiming would equally counteract external pressure on women not to join; and
- special benefits might make up for discriminations in other fields that lead to lower pension entitlements, mainly lower participation in waged employment and lower wages. Western pension systems include various examples of such provisions, including a minimum pension, a pension supplement for people with a long employment biography but low wage (mostly women), or special pension supplements for having raised children.

There is one aspect that is largely beyond the reach of Government: the distribution of resources and power within the household. It is not always or not only due to legal regulations if a man joins the pension scheme while his wife does not (Box 28). It also depends on the way the spouses negotiate their daily business. It also depends on the individual couple if in old age they share the husband's pension on equal terms or not. It is also worth investigating how families use the different forms of allowances available under family planning schemes. Which family member uses the money for what purpose?

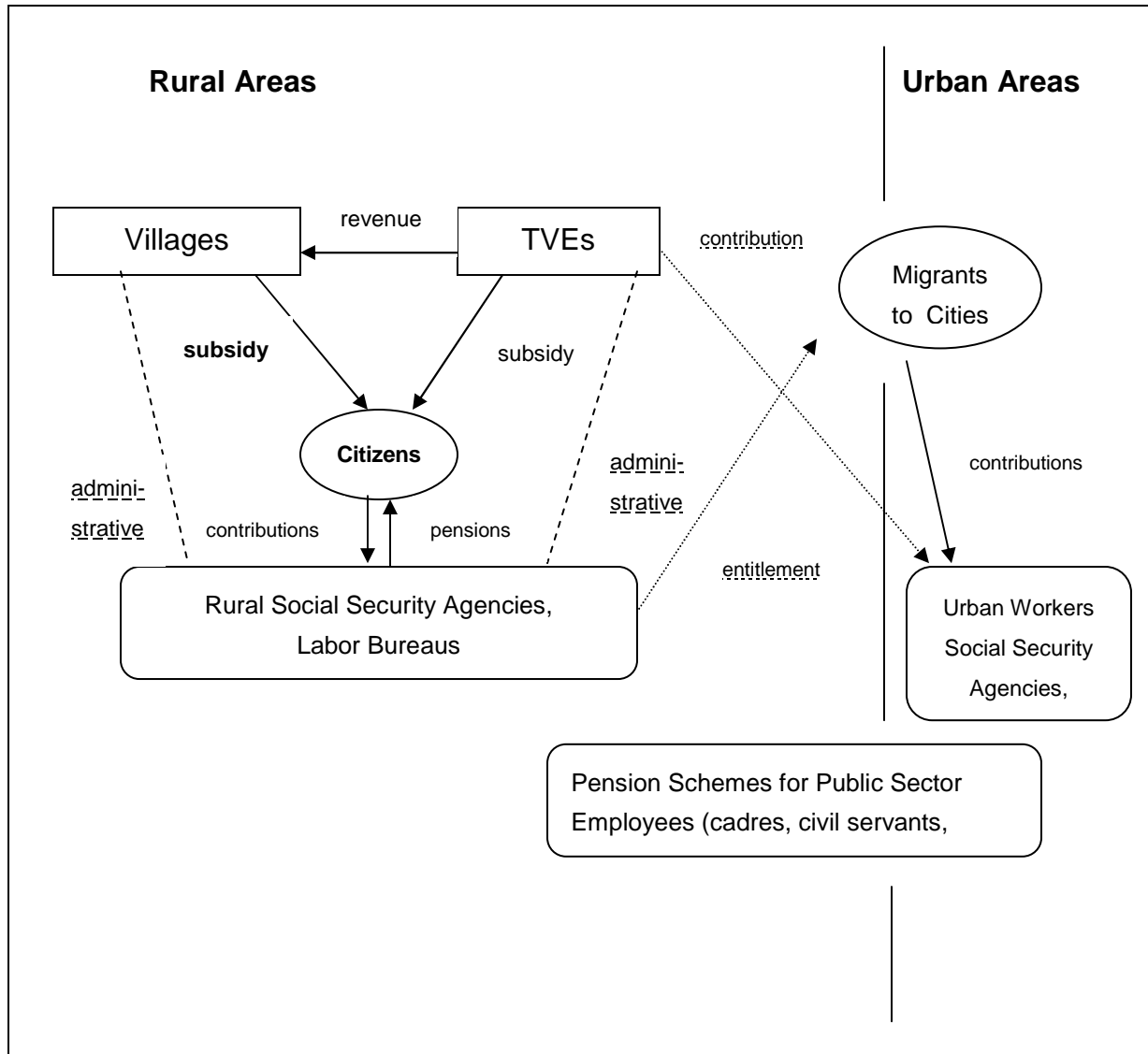
4. Conclusions for Pension Reform: The Road to Social Insurance

The emergence of TVEs has transformed the rural economy. It is also transforming rural old-age security. TVEs and the village self-government have seized the new rural pension scheme and developed a kind of symbiosis with it. Migration to cities adds to the changes.

This shows, first, that there is a demand for pensions in the countryside, not only from the side of the rural citizens but also from political and economic institutions. The institutions take an interest in pensions. Second, the institutional links that have built up between pensions,

TVE, and village go beyond the idea of organized individual saving that informed the rural pilot schemes. A complex new institutional structure of old-age security has emerged (Figure 5).

Figure 5: Old-Age Security in Rural Areas—A Complex New Institutional Structure



Our thesis is, this newly evolving institutional arrangement points at more developed forms of old-age social security, as found in urban areas or in social insurance schemes in developed countries. Four elements testify to the modern character of the evolving structure.

- Employers play a role in social security by paying subsidies, sometimes also by taking part in the administration of the scheme (collecting contributions and transferring them to the state administration of the scheme), or even by organizing their workers to join.
- Employers make use of the scheme to serve their economic interests. It has become part of their corporate policy.

- There are elements of redistribution, organized both by TVEs and villages, to profit special merit groups and self-vested local elites.
- Pensions under the rural pilot scheme, which vary greatly from village to village, are partially superseded by more standardized schemes to allow for labor mobility. TVEs and migration to the cities are feeding people into the urban pension scheme, thus blurring the boundaries between rural and urban social security.

However, the newly evolving structure is growing wild, lacking coherence and rules. In the interest of rural citizens and as the rural economy, reform is urgently needed.

The following principles of reform rest on two premises: First, they build on existing elements of the new structure, aiming to clarify rules and to consolidate the system. Second, they derive from generally accepted criteria of economics, law, and social policy.

The question is not so much whether to unify the rural and the urban pension schemes or not. It is the institutional design that counts. Rural schemes may adopt social-insurance-like characteristics without merging with the urban schemes. The current arrangement of old-age security in the rural PRC contains the germs of modern social insurance. If politicians, administrators, and citizens want it, the system can be developed toward social insurance as outlined below. This would be a further step toward undivided citizenship in the PRC.

5. Principles of Consolidating Old-Age Security in Rural Areas Toward Social Insurance

a. Economic Principles

- i. Whenever there is an employer, the employee should participate in a pension scheme and the employer should contribute**

Set up rules for contributions, benefits and subsidies that bind both sides.

This principle aims to create fair and equal competition among enterprises. No enterprise shall be allowed to refuse social contributions to lower its production cost.

The principle would also prevent villages from interfering at will with the business of their TVE. Currently, villages use TVE profits arbitrarily for contributions to villagers and local elites. They also close the labor market by refusing contributions to nonvillage workers.

Such reform would be part of a more market oriented industrial policy and TVE reform.

- ii. Introduce a two-layered-pension scheme, with a public and an occupational layer**

Currently, some employers are reluctant to join the scheme to evade contributions, while others see it as a productive means of organizing their labor force. A two-layered scheme can react to both, by forcing reluctant employers into the scheme (compulsory bottom layer) while allowing interested employers to top it up (voluntary top layer).

In this way, public and occupational schemes would be clearly distinguished. Currently, employers misuse the public scheme as an occupational scheme.

b. Legal Principles

i. Treat employees who do similar work alike

They should be covered by similar pension schemes (or by the same scheme). Ownership of the enterprise (TVE, SOE, COE, private, foreign), area (rural, urban, town, small city, city), and household registration (*hukou*) (agricultural, nonagricultural) should not matter.

Currently, people doing similar work are often treated differently. TVE employees, but also persons in the rural service sector like gatekeepers, electricians, or shop assistants, often have no or only a small pension. They also have to work beyond the age of 60 or 70, while urban employees in the same jobs can enjoy retirement and a good pension.

A reform of the household registration system (*hukou*) is part of a general legal reform. The current system is increasingly at odds with the real situation of the individuals. In the field of social security, it should be replaced by the employment status as criterion of eligibility. This would also foster the mobility of labor.

ii. Treat the self-employed alike

They should also be treated without regard for their status and area. Currently, the urban self-employed are targeted to be included in the urban workers scheme while the rural citizens working on land, who are also self-employed, are excluded from any system, except the rural pilot schemes. Some Western countries chose to include farmers in schemes for the self-employed (chapter 4.D).

c. Social Policy Principles

i. Standardize the key parameters of the pension system: contributions, benefits, subsidies, and administrative procedures

This does not mean making everything equal. Villages and TVEs are very diverse across the PRC, even within one county, so that diversity should be allowed for in social security.

However, under the current rural schemes, the key parameters are undefined and left to the participants, to the village and the TVE. In this way it is impossible to secure objectives of social policy like security, poverty reduction, and equity. Inadequate benefits, social exclusion (e.g., of women due to informal registration procedures, Box 28) and misuse by local elites (regressive redistribution, Box 26) abound.

ii. Define clear and explicit criteria of redistribution

Redistribution is a key element of social policy that needs criteria and rules. Currently, redistribution exists but people are not aware of it. There is selective privilege and disprivilege determined by local elites. This should be replaced by explicit criteria decided by reference to general norms.

D. The Economic and Political Environment of Pension Schemes

Setting up pensions is not only about an equitable design of rules for benefits and contributions. Pensions are embedded in society. This section, therefore, focuses on two questions.

- What is a favorable environment for pensions? What economic, social, and political conditions have to be met for pension schemes to operate smoothly?
- And vice versa: What effects on their environment do pension schemes have? Do some schemes have negative effects, e.g., on the economy, or maybe even positive effects? This will depend on the design of the scheme.

We look at three environments: the economy, patterns of individual behavior and government policies.

1. Economic Conditions

The state of the local economy is obviously a prime condition for the creation and the sound operation of a pension scheme. The basic dilemma is that in areas with most poor people there tends to be least government revenue to meet those needs. In principle this problem can only be tackled by a higher level of pooling of insurance funds to achieve redistribution between areas and groups. Government subsidies might add to that. A second, analogous dilemma concerns mutual aid. In the rural PRC, poverty tends to cluster so that poor people live among other poor people who lack resources to help financially, especially if a collective contingency like drought or flood has affected all of them.

Under the current pilot schemes that are based on individual savings accounts with limited elements of redistribution, poor people in poor provinces are doomed to remain in poverty even in old age. Poverty is a main reason for nonpayment of negligible contributions. Moreover, in poor people's lives there is no phase of retirement. They are normally forced to work in old age till they are entirely incapacitated. Although there is generally no strict notion of retirement in the rural PRC—meaning a standard age at which people give up wage labor or subsistence production—citizens who live above the poverty line do give up work at the age of 70 at the latest.

The dilemma is reproduced in the structure of taxation for the elderly. The poorer a province and its population, the higher the relative tax burden on its elderly. In Yantai Municipality, Shandong, taxes for the rural elderly are reduced from the age of 70. In Hubei Province, although less well-off than Yantai, the age threshold for tax reductions is 65 years. For people aged 60 to 65 there is a partial reduction. But for the poorest province we visited, Yunnan, the reduction starts only at the age of 80. This is inequitable and could hardly be justified on moral grounds or by reference to moral hazard.

Yunnan Province is a case in point. The provincial administration of the public pension scheme is sound. Its administrative structure is similar to that of more developed areas (Chapter 6.B) and government officials have been very active in promoting the scheme all over the province. But they achieved a coverage rate of only 4% of the rural population. The province is very poor, with low incomes and few TVEs. Huapo Village in Wuding County demonstrates the situation—seemingly a lost cause for public pension schemes (Box 31).

Box 31: Pensions under Extreme Poverty

Huapo Village in Wuding County (national poverty county), Yunnan

The village lies in a remote high area up in the mountains and consists of 305 households. The name—meaning slippery slope—indicates that conditions for farming are limited. The farmers grow only corn. The next town is 8 kilometres away. Average net income per person in the village is 100–500 yuan per year. Out of the 305 households, 70 currently receive Poor Relief, a very high proportion.

The public pension scheme was introduced in the village in 1996. Since the administrative village was too poor to pay subsidies, the matter was delegated to the level of the natural villages (groups). Three out of the nine natural villages decided to join the scheme, though only one of these could pay subsidies. Asked about possible future developments, a village leader said that in case of sound economic development 50% of the farmers might be able to join the scheme in 2010. He himself has no pension entitlements ("because in 1996 I was not yet village leader"), which evidences the poverty of this village.

Two villagers exemplify the problems: a young widower, aged 35, who can hardly secure subsistence, said he was forced into the scheme and paid a once-in-a-lifetime contribution of 300 yuan for his 6-person household, with a 50 yuan subsidy by his natural village. The individual pensions to ensue from these contributions will be close to nothing. Another young man, also aged 35, has no entitlements because his natural village did not join the scheme. In the future, he said, he might buy a pension even without subsidy if he should have money. His expectations are very limited: He would use the pension to buy salt and medicine. This village seems to be a lost cause for a contribution-based social insurance scheme. It is equally lost for commercial insurance—sales agents never came anywhere near this village.

However, very poor people, as described in Box 3, may be included formally in a general old-age security system that would include subsidies from government and, through pooling, from better-off areas to allow very low basic benefits. The minimum living standard system may also be applied. Inclusion in some national scheme would at least symbolize that they have not been forgotten—that they are recognized, even at low level, as citizens of the PRC. We may conclude that there is a case for public pensions all over rural PRC. But different regulations would have to be applied. Rich areas can take the lead while poor areas can be included symbolically.

However, policies that further the infrastructure and the economic situation of the area as a whole have priority over policies that aim at individual households. In the future this may include a decision to close down unprofitable land and to encourage these farmers to change to a different kind of work.

In better-off areas more could be done. Ten well-off coastal provincial units could take the lead: Beijing, Tianjin, Hebei, Liaoning, Shandong, Shanghai, Jiangsu, Zhejiang, Fujian, and Guangdong. Their socioeconomic conditions are conducive to a formal arrangement for farmers' old age. Both the employment structure and the age structure are favorable.

The eastern economic region in the PRC normally includes 12 provincial units. They are Beijing, Tianjin, and all coastal provinces. Per capita GDP in Guaxi and Hainan, however, is

much lower than almost all the other provincial units except Hebei in the region. Therefore, these two provinces are less suited to start together with the others.

The Eastern Region (referring to the 10 coastal provincial units) is richer than the rest of the country and, at the same time, has to care for fewer dependent persons, although its elderly population is increasing more rapidly than the poor areas. Moreover, the rural households and population are becoming more dependent on nonagricultural activities or wages. Therefore, it is not only desirable for the current rural working population to prepare for their old age, but they also have the capacities. The Government should act now to help them prepare for their future.

Tables 20 and 21 amplify this finding.

Arable land. Both total population and rural population in this region consisting of the 10 provinces account for about 36% of the national total. However, arable area in this region accounts for less than one quarter of the national total. Per capita arable land in the selected rural sector is only equivalent to a little over two thirds of the national average.

Nonagricultural work. The first agricultural survey made in 1996 showed that many households and working populations in the Eastern Region are getting involved in nonagricultural activities and industries and that the more developed the region becomes the more rural citizens depend on the nonagricultural sector.

Wages. Table 20 also shows the growing reliance of rural households on wages. In the selected rich provinces in general, a little less than half of the net incomes were from wage incomes compared with the national average proportion, which is 28.5%. In Shanghai, the richest province in the PRC, wages account for more than three quarters of net incomes. In the least developed provinces among the group such as Fujian, Shandong, and Guangdong, it is slightly above 30%.

Dependency ratios. Table 20 shows that the old-age ratio (number of elderly per 100 persons of working age) is higher in most of the selected provinces than the national average. On the other hand, the total dependency ratio (elderly plus children) is lower than average. Therefore, it may be wise for these provinces to begin preparing for the rapid ageing now when the overall number of dependent persons per labor force is still low.

Guangdong and, to a lesser extent, Fujian are exceptions. Although their economies do much better than national average, their dependency ratios are higher than the national level. This is mainly due to poor implementation of the family planning policy. Figure 6 illustrates the negative correlation between local economic development and birth control, i.e., higher economic development goes along with lower birth rates. Guangdong clearly is an exception.

Migration from the countryside to the coastal provinces further "refreshes" the population, bringing in more young people. However, the low birth rate predicts ill for the future. Whereas it may be welcome at present to reduce dependency "burdens," it will make the population age more in the future. In this way the highly urbanized coastal areas may be heading toward the same problem—low birth rates and, decades later, high overall dependency ratios—which is already haunting Western societies.

Table 20: The PRC's Eastern Region—Demographic and Economic Conditions, 1999

Region	Population		Dependency Ratios (rural)		Birth Rate	Per capita GDP (yuan)	Per Capita Net Incomes (rural households)	
	Total (rural and urban; millions)	Agricultural (% of total)	Elderly (%)	Total (elderly and children, %)			Total (yuan)	wages (% of total net incomes)
National	1,259.1	74.49	10.85	49.0	15.23	6534	2,210.34	28.51
Eastern Region Total	456.3	60.80	12.10	47.10	10.36	1,3754.5	3,470.29	46.64
as % of national	36.2	81.62	111.52	96.12	68.0	210.51	157.0	163.59
Beijing	12.6	32.25	11.89	36.13	6.50	19,846	4,226.59	61.53
Tianjin	9.6	42.01	10.51	46.81	9.68	15,976	3,411.11	42.35
Hebei	66.1	81.02	9.71	46.53	12.99	6,932	2,441.50	36.71
Liaoning	41.7	54.26	8.55	36.56	10.38	10,086	2,501.04	32.64
Shanghai	14.7	26.16	15.18	35.29	5.40	30,805	5,409.11	77.50
Jiangsu	72.1	71.05	14.17	44.25	10.50	10,665	3,495.20	46.37
Zhejiang	44.8	78.79	13.52	41.07	10.64	12,037	3,948.39	44.01
Fujian	33.2	79.63	12.08	54.60	11.06	10,797	3,091.39	31.74
Shandong	88.8	73.98	12.52	45.08	11.08	8,673	2,549.58	31.03
Guangdong	72.7	68.81	12.36	60.26	15.32	11,728	3,628.95	30.43

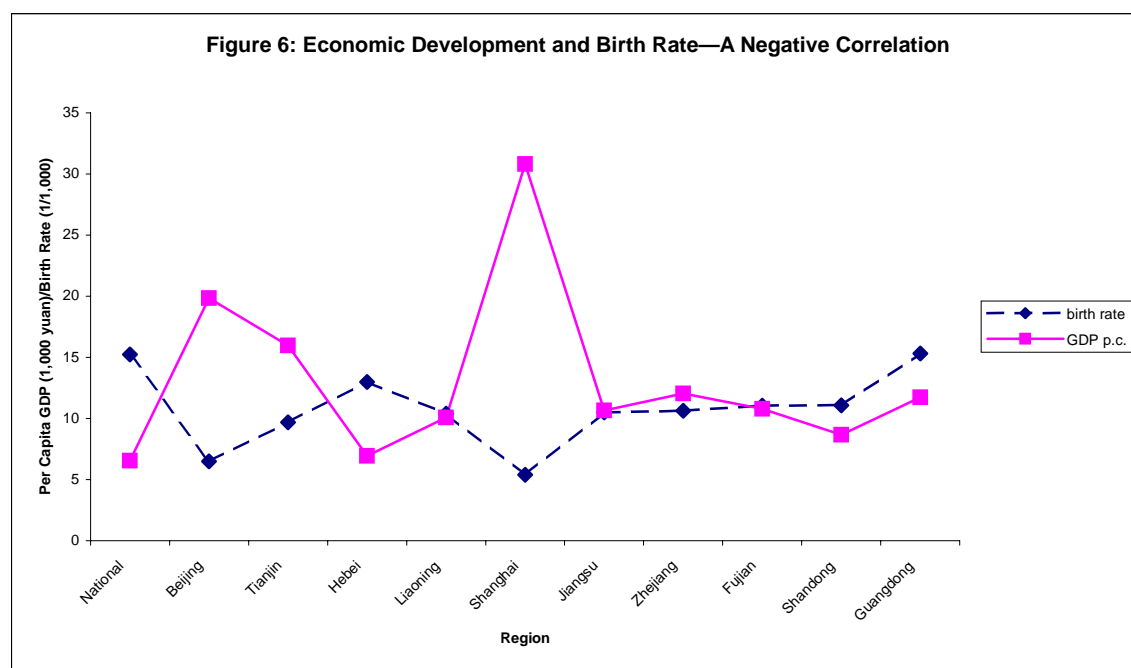
Source: National Bureau of Statistics, Department of Demographic, Social, Science and Technology Statistics.

Table 21: The PRC's Eastern Region—Arable Land and Economic Activities of Rural Households, 1996

Region	Rural Population (million persons)	Per Capita Arable Land (hectare)	1.1 Rural Working Population			Rural Households (hukou)		
			Total (persons)	Agricultural Labor (%)	TVE Employees (%)	Total (number)	Nonagricultural (%)	Primarily nonagricultural (%)
National	873.8	0.149	528,805,904	81.97836	10.02	213,827,500	9.70	22.49
Eastern Region Total	313.7	0.101	174,747,114	75.49668	17.81	78,865,749	16.95	35.78
... as % of national	35.90	68.08	33.05	92.09	177.71	36.88	174.74	159.09
Beijing	3.8	0.091	1,463,127	67.80	53.69	1,035,368	44.61	66.31
Tianjin	3.8	0.129	1,825,769	70.33	42.30	979,260	27.23	50.20
Hebei	51.7	0.133	29,780,248	82.56	8.96	12,802,814	8.58	23.25
Liaoning	21.6	0.194	13,391,906	83.41	11.78	5,916,087	9.97	23.56
Shanghai	4.0	0.079	1,651,923	58.81	100.80	1,175,862	48.74	73.81
Jiangsu	53.3	0.095	30,746,586	69.22	20.39	14,028,282	19.86	45.41
Zhejiang	33.8	0.063	16,320,651	64.06	28.50	9,203,182	34.61	57.05
Fujian	24.5	0.059	13,027,185	71.68	11.40	5,423,064	17.01	41.26
Shandong	68.7	0.112	42,902,355	82.88	11.40	18,237,252	7.74	19.99
Guangdong	48.5	0.067	23,637,364	68.91	26.91	10,064,578	20.57	42.68

Note: Percentage of township and village enterprise employees may exceed 100 due to floating workers.

Source: National Office of Agricultural Survey.



Up to this point, we have dealt with the economic requisites of setting up a rural pension scheme. Putting the reverse question: What effects do pensions have on the economy? Effects

on economic behavior will be analyzed below. (Positive) effects on rural industry have been analyzed in Chapter 6.C. However, the current schemes are so little developed that an econometric model of the future impact on financial markets and investment, unlike for the urban scheme, would have to rely on numerous theoretical assumptions. This is beyond the scope of this report.

2. Patterns of Individual Behavior

Joining a pension scheme, public or private, requires much from people.

- *Ability to pay contributions.* Those who barely secure subsistence cannot join. We analyzed this problem in the preceding section as part of the economic environment of pensions.
- *Willingness or inclination to pay.* Even if some money is left after paying for basic needs, people may not want to spend it on contributions. They may have alternative choices. It is a matter of preferences.
- *Trust.* Even if they would both be able and willing to join, they may not want to entrust their money to the institution that runs the pension scheme, be it a governmental agency or a private company. Trust is a crucial requisite of pension schemes.
- *Discipline of spending behavior.* People may be able and willing to join and may trust the agency but they may be unable to budget in a way that money is left for contributions. Short-term inclinations prevent these people from taking a longer view. Disciplining oneself and taking a longer view has been seen as an essential part of modernization (Chapter 3).

All four requisites are not to be taken for granted in the PRC, as evidenced by the low participation in the rural pension scheme. In the following paragraphs we will demonstrate by evidence from the field visits why these behavioral requisites are critical and what could be concluded for pension reform and other policies.

Willingness to pay (problem of preferences. People with a fairly low income often could pay contributions (or pay more than they actually do) but, when questioned, alternative preferences come to the fore. In our interviews we came across a broad range of spending items that were competing with contributions for old-age pensions. These seemed to be fairly rational choices. When asked, people could normally give the following reasons why they preferred a certain item to contributions for pensions (Box 32).

- Spending money on medical services in case of ill health of a family member or providing for such cases by private insurance is a paramount concern of all our interviewees. Since medical services have to be paid for, medical impoverishment is a constant threat to many people.
- Education has also a high priority in people's budget but it is often very difficult to afford. Even if formal schooling is free for a certain number of years there are expenses like books, special charges, or, in case of remote areas, accommodation.
- People buy an accident insurance for themselves or for their children.
- They may also save money in a bank to provide for the above-mentioned needs or other contingencies. Unlike pension contributions, savings are available when money is needed for other contingencies than old age.
- Money may also be invested as risk capital, for example, buying a car or a boat to set up a business. Sometimes parents do this for their children (Box 33).

Box 32: Paying Contributions—Competing Preferences

A young family, Jiuchang Township, Wuding County (national poverty county), Yunnan

The couple works and has two children, aged 4 and 7. The husband works as a group leader in a brick township enterprise. He earns 5,000–6,000 yuan per year and his wife 2,000–3,000 Yuan. They spend their income like this.

- He made a once-in-a-lifetime contribution to a public rural pension scheme of 250 yuan, supplemented by a 50 yuan subsidy from his village. This amount is negligible and will only result in a small benefit in old age.
- His wife has no pension; she has not paid into the scheme.
- They have no commercial insurance of whatever kind.
- They spend nothing or almost nothing on housing because they preferred, despite their high income, to live with their children in one room in a factory building that looked like a slum.
- But they save 4,000 yuan per year, in a bank. This is their main priority in spending money.
- For food and subsistence they spend 3,000 yuan per year.
- For education they spend 700–800 yuan per year, including 300 yuan for textbooks, 80 yuan for accident insurance for one child, 60 yuan tax for items like paper, bags, etc.

Their savings shows that they are future-oriented. But why does he pay so little for his pension? He said that he wants to prepare for emergency cases like illness of a child. Money in the bank would be immediately available in that case. He does plan his retirement—even at the early age of 40, due to the hard work in the brick factory, returning to his land—but he does not want to secure his retirement by a substantial pension. His priority is to save as much money as he can and to use it later in some way, maybe by buying commercial pension, to secure his old age, in combination with support from his children.

We may conclude that even workers who are better-off (in this case compared with the low standard of Yunnan) may not want to pay much into a public pension scheme while providing for their future by saving considerable sums.

Box 33: Economic Risk Behavior Competing with Preparation for Old Age

A middle-aged woman in Qunguang Village, Huangpi County, Wuhan Municipality, Hubei Province

She is 48 years of age, works the family land (1/2 mu), has a son and two daughters, aged 20, 18, and 16 years, respectively. In 1993, she and her husband spent 40,000 yuan for three boats for their business of transporting sand. As there was no demand, the money invested was spent in vain. While they belonged to the better-off families of the village before, they now rank among the least well-off group. The children, who do not work on land, have no regular employment, and the husband's business is also insecure. Their son once went to Shenzhen to seek employment but failed. Besides a tiny life insurance for accident and death for both spouses, they have not provided for old age nor for ill health. She desperately needs surgery that would cost 5,000–6,000 yuan, which she could not afford.

The couple practices risk behavior suited to the opportunities that open up in the PRC market economy. If she had not spent the money on the boats, she would still spend it in a similar way, namely, on a car for her son to run a business.

Under a compulsory pension scheme these people, before their failed investment, would still have had enough money left besides paying contributions. Contributions would not have severely competed with risk expenditure for business. On the contrary, compulsory social insurance (for old age and for ill health) might have provided a security net, a firm basis from which they could build their risk behavior. In this way, pensions could support modernization.

The examples given in the boxes suggest that the behavior of the persons is rational. They do provide for vital contingencies or spend on seizing opportunities that are more urgent to them than old age. They do not spend shortsightedly but they plan for the medium term. In a time of upheaval this may be rational. Nobody knows what pension they might get in 30 years' time, and they may not even need it since family support and land still have at least some capacity as sources of last resort.

Two conclusions can be drawn.

First, one might consider making participation in a pension scheme compulsory, at least in better-off areas, where people can afford contributions. It may have been wise to start the MOCA scheme in 1991 based on voluntary participation. Today, about 10 years later, however, the awareness among the rural population of the importance of providing for the future has increased.

Second, it should be made sure that other vital concerns like health and education are not thwarted by compulsory contributions to pension schemes. This is a challenge for policies on health and education. The fulfillment of these basic needs should not depend on income. It is also a question of the design of the pension scheme. Some forms of providing for old age, especially life insurance, may be used to get a loan to provide for contingencies that occur before pensionable age. An alternative would be to embed old-age pensions in a package of social insurances that would also cover health and accident. The group that evaluated the MOCA pension scheme in 1995 (Chapter 6.B) already made a similar point, based on what farmers themselves named as their most urgent needs. A minimal solution would be to cover

such contingencies partially under the Minimum Living Standard System (MLSS) as done in Yantai.

Trust. While many people are sympathetic to pensions and do participate in the scheme, many of our middle-aged interviewees expressed concern about their future pensions. Two worries prevailed:

- a crisis in the financial market might devalue pension entitlements, and
- government policy might change.

Politics can do little about the first concern. Volatility of financial markets is a weak point of funded pensions. Good regulation by the Insurance Regulator and other regulatory bodies (Chapter 6.E) may only dampen this insecurity. The second concern, however, is within the scope of Government. In the face of the diminishing political support for the pension scheme, some farmers have even left the scheme. They have more trust in the urban pension system that, as they told us, has more support by Government.

Discipline and long-term view. In the course of modernization, people plan their lives more than before in a longer view (Chapter 3.B). According to our field visits, rural PRC seems to be halfway in this respect. People do plan their lives but rather in the medium term. As seen from the above cases, they save, provide for possible illness and for the educational career of their children, or they invest in business. Similarly, citizens join the public pension scheme mostly in view of short- or medium-term gains, namely a subsidy by their village or TVE and the promised interest rate above the rate attainable for a bank deposit. The small amounts of contributions paid by many participants do not point at a strong commitment. There is only scattered evidence as yet that the system of providing for old age by individual accounts has strengthened the consciousness of providing for one's future, as assumed by Wang (1996). As said, this may be rational in a fast changing society.

Among the younger people, however, we find signs of an emerging 'modern' lifestyle that includes taking a long-term view of life: The idea of retirement hitherto unknown in the rural PRC crops up (Box 13), and a young woman (Box 14) does not want her own plot of land but makes regular high contributions to the pension scheme instead. As regards the elderly, the desire not to be dependent on one's children may have existed before but could not be realized when resources were scarce. The quest for individual autonomy typical of modernity is likely to strengthen this desire.

3. The Policy Environment

Chapter 6.C showed that a good economic policy, including industrial policy towards TVEs and labor migration, is crucial for old-age pensions, and that vice versa, pensions can support rural industry.

There are three other fields of policy which are closely linked to the rural pension schemes:

- health policy and educational policy,
- central policy toward old-age security, and
- agricultural policy.

The first two are putting rural pensions under pressure right now, whereas, agricultural policy is a more general context of pensions that is likely to become immediately relevant only in the near future.

Health and education. As described above, many people cannot afford health and education, and when they spend there is little left for paying into pension schemes. This clearly mirrors the failure of recent policies in the countryside. All places we visited reported a high proportion of "medical impoverishment." Most officials said that 80% of poverty was caused by illness, a figure taken from a publication by the MOCA. But they confirmed that in their area medical impoverishment indeed accounted for most of poverty. Very poor people do without medical treatment even when they are severely ill (Box 11).

Education is also expensive. In Huapo Village in Wuding County, Yunnan, we were told that more than 20% of the children of both sexes do not attend school. Health and education policy is more immediately pressing than pension policy.

Central policy toward old-age security. As for health, the citizens' problems mirror flaws of policy. As described earlier, the recent erosion of trust in the pension scheme is largely caused by lack of support from the center. Not only the participants but also the local administrators are demotivated. We found this in all counties visited.

The first critical event was the transfer of the pension administration from MOCA to MOLSS at all levels of Government. When the rumor of the imminent transfer spread in late 1997, the local officials reduced their commitment. They gave up actively promoting the scheme. In turn, this reduced farmers' support of the scheme. The problem is especially severe in Hubei where the scheme is still run by the civil affairs bureaus. The provincial government eventually decided in April 2001 not to transfer administration to MOLSS. There is no commitment to the scheme any longer.

The second critical event was the sign given by the Center in the late 1990s that the scheme should be stopped (Chapter 2.B). Since this news spread to the localities, inactivity and resignation prevailed. No definitive decision is in sight.

The administrators we interviewed at the county, town, and village levels called for a signal by central government to show commitment to rural pensions. Such signal would include

- passing a law on rural pensions,
- making participation compulsory,
- giving subsidies,
- granting tax deductions for contributions, and
- resuming active campaign for pensions in the countryside.

Agricultural policy. The future of rural social security is linked to structural changes in the rural economy. The PRC policy relies on land as a system of social security (World Bank 1997b). Land is used by farmers for subsistence, not only for selling in markets. This system checks the commercialization and "marketization" of agriculture. It also reduces the need for modern formal social security.

However, the use of land for subsistence and its use for commercial production are not mutually exclusive. In the theory of developing countries, early dualist approaches sharply

distinguished between modern capitalist production for the market and traditional production for subsistence (or in an informal sector). The traditional sector was seen as merely backward, underdeveloped, unproductive, and as a hindrance to the emergence of markets. Other scholars, by contrast, emphasized the interdependence and linkages between subsistence production, informal sector, and formal market sector. The traditional sector is seen as vital for the farmers both in economic and sociocultural terms. It serves to secure survival and security for those who work on it (Elwert/Evers/Wilkens 1983). According to these theories, the pursuit of security prevails over the maximization of profit.

This theory can be applied to the PRC although in a special way. An informal sector is less developed because of a high level of state regulation. However, households and groups of households operate in local markets and, at the same time, produce for subsistence. The state allocation of land, the attribution of *hukou*, and fixing of grain prices regulate this system. With the introduction of the household responsibility system in the 1980s, production for subsistence and commercial agriculture could be profitably combined. For a period of transition this seems to have provided a feasible way of rural development, confirming the theories of interdependent and interlinked economic structure.

Sometime in the future, however, the tension between subsistence and commercialization may become too high. In the view of the World Bank (Nyberg/Rozelle 1999), the growth potential of the current household responsibility system is nearing exhaustion. Reform will be needed to pave the way for full commercialization. This may happen soon when the PRC agriculture will have to face the world market.

Three conclusions can be drawn for pension policy.

- With the increase of commercialization and the decrease of the social security function of land, the need for modern formal social security will become more urgent. In all Western countries, formal forms of social security have replaced traditional forms (though other traditional forms than land, above all family support, still play an important and new role in many respects).
- By limiting the commercialization of agriculture, the PRC government currently reduces the need for a formal arrangement for old age. Although the use of land for subsistence is already eroding (Chapter 6.A), land can still be referred to in political rhetorics.
- Pensions for farmers do not only mean doing good. They can also benefit the economy. When full-fledged commercialization of agriculture will be on the political agenda, old-age pensions and other social policy measures can be used to support and accelerate the change. In Chapter 4.D we showed how European countries used pensions for farmers to raise productivity in farming and to absorb rural surplus labor.

E. Is There a Case for Commercial Provision?

The idea of putting more emphasis on commercial elements in the management and/or the provision of public services is currently looming large in the PRC debate, not only in rural pensions. The ADB report on urban pensions has analyzed in detail the issues of fund management, financial markets, and regulation. This section concentrates on aspects that are specifically relevant to rural pensions, although some points could also inform the urban debate. The question is, is there a case for commercial providers in the rural PRC?

In the debate about the future of the rural pilot pension scheme, the idea of letting commercial insurance take over the scheme has come up over the last two years. Recent MOLSS blueprints seek a middle ground by outlining a combination of public and commercial administration (Chapter 2.B).

Privatization' has been one direction of change in Western countries, although the core of the welfare state has mostly remained public. Commercialization in the PRC, is not quite the same because commercial companies in the PRC are owned or heavily regulated by the state. Still, some questions are similar.

Commercialization in old-age security can mean something very different

- *Passive commercialization.* It can simply mean government inactivity: letting anybody take up commercial insurance or private pension plans if he/she can. Government would neither care for those who cannot, nor seek to regulate the supply side of private pensions. This simplified idea is tempting to politicians.
- *Active commercialization.* It can mean an active policy of creating a market for financial services and commercial providers, by comprehensive regulation. This concept is widespread in the PRC and regulating agencies, like the Insurance Regulator, receive much political attention. The idea is that the market will provide better and cheaper products and a more efficient administration. The state may also enter a partnership with commercial providers to create a certain product.
- *Commercial fund management.* Commercial elements can be restricted to the management of funds of public schemes. The idea is to maximize returns while the product is defined by the state. This differs from the second version that goes further by letting the market create new and more looked-after products. This view is even adopted by some persons who want to keep the basic organization of social security public.

The second and third versions are public-private (or public-commercial) partnerships. In Chapter 3.A, we argued that it is misleading to present public or private as a choice between two options. In reality it is mostly a mix of both. Even in the first version, some less visible government support for commercial schemes is normally involved.

In rural areas, commercial provision as well as public-private partnerships are not new. Right from the start in 1991, the public pilot schemes faced fierce competition with commercial insurance companies, which started business even before 1991. The pilot schemes even changed some of their rules in response (Chapter 2.A and Table 5). There were also partnerships between the state family planning agencies and commercial insurance.

In the rest of the section we aim to clarify two points.

- Does previous experience with commercial providers in rural areas suggest that commercialization could be a viable path in the future?
- What risks are involved in commercialization and how could Government handle these risks? This is the question of regulation.

1. Previous Experience: The Limits of Commercialization

Generally, private insurance and other financial providers have little interest in the rural market. Transaction costs are high because farmers live in scattered villages and the area is often mountainous. At the same time, individual contracts tend to be small.

Commercial providers have the same problem like public provision, namely poverty of the farmers and difficulties of local delivery. However, both can cream the market by concentrating on better-off farmers in areas with good infrastructure.

In every county we visited we spoke to local officials from commercial insurance companies. The general assumption was confirmed: Commercial providers take little interest in the rural market, except for some creaming. In fact, they are retreating from rural areas. In poor areas no sales agent has ever turned up.

How did the public-commercial partnership between the state family planning authorities and commercial insurance work out? The experience is not encouraging either (Box 34). Apparently these problems are not caused by mismanagement or individual failure. They point at structural limits to commercial provision in the countryside. Previous experience, therefore, does not suggest that commercial provision could be a more far-reaching solution for the countryside.

Box 34: A Public-Commercial Partnership: State Family Planning Subsidizes Commercial Insurance for One-Child Families

In Yantai, the state family planning authorities subsidized commercial insurance for children of one-child families by 10 yuan per month through payment by the village. The insurance pays money in case of accident or when the child reaches the age of 14. This public-commercial partnership started in 1988. The scheme was initially successful but is now drastically decreasing.

The commercial providers are no longer interested because what was good business for them in 1988 is now, since their company operates on a larger scale, too little. In addition, administrative costs were too high (high transaction costs).

The scheme is seen as a burden also by the families because, with increasing participation, the family planning authorities asked them also to pay contribution, which was not easy for the families to do regularly. They preferred cash to subsidies.

In Muping County the scheme was stopped as early as 1997 for this reason was replaced by a monthly allowance of 5 yuan. In the poorest county visited, in Wuding, Yunnan, such scheme never existed. One-child families get a general allowance of 60 yuan per year.

How, then, could a takeover of the public pilot schemes by commercial insurance look like? We put this question in every locality.

Some companies admitted that the deal would not be interesting for them. The China Life Insurance Company (CLIC), Muping Branch, said that the serious abuse of pension funds and the promise of very high return rates made under the MOCA scheme would make business

too difficult. Another insurance official pointed at the different nature of commercial insurance and rural old-age security. After a transfer, he feared, the business might still be subject to government intervention.

These statements accurately reflect some of the problems involved. Commercial companies that would have to do the job can be wiser than some politicians.

The China Life Insurance Yantai Branch, however, would welcome a takeover because they have accumulated much experience and have sufficient branches and office at the township level. Similarly, the China Life Insurance Hubei Branch informed us that although they have shifted their focus to the more profitable sector, i.e., the urban areas, they would have the capacity to take over for three reasons: their rich experience, the existence of an administrative network, and because they have designed new investment products.

What about administrative costs? Some people expect commercial providers to operate cheaper than state bureaucracies. Here, too, the answers differ between the companies. Administrative costs may be higher than in the current public schemes (Box 35). This would confirm international experience. An official from the China Insurance Regulator also suggested that a commercial insurance for farmers would be very expensive. Neither would social insurance in the normal sense be viable for the majority of farmers. In his view, mutual insurance could be a good alternative.

**Box 35: Estimated Administrative Cost of a Takeover of the
Public Pension Schemes by Commercial Insurance**

For Muping District, based on information by insurance companies

A. Size of Administrative Staff

1. Takeover by a commercial company without township offices such as Pingan or Pacific

County level:	At least one office worker needed for the new business.
Township level:	At least 6 new offices have to be established. They should employ 30 staff members.
Total:	At least 31 staff members should be employed at the two levels. That is to say, almost all current staff members (36, 15 at the county level and 21 at the township level) for the MOCA/MOLSS scheme in Muping could be taken over. The problem is that some of them would have to work at the countryside.

2. Takeover by the CLIC Muping Branch

County level:	1 person.
Township level:	12 staff members.
Total:	13 members. That is to say, the China Life needs only about one third of current staff members to carry out the schemes.

B. Administrative Cost

Takeover by Pingan or by Pacific office at county level and 6 offices at township level

County level:	30,000 yuan
Township level:	18,000 yuan (6,000 yuan x 3) 40,000 yuan (20,000 yuan x 2) 20,000 yuan 78,000 yuan per office
6 offices:	468, 000 yuan (78,000 yuan x 6)
Total:	498,000 yuan (30,000 yuan + 468,000), equivalent to 7.1% of current annual contributions.

All in all, previous experience and estimations based on the current operations of commercial companies do not suggest that commercial providers could take a substantial role in rural old-age security. Key points include the following.

- Due to increasing competition in the life insurance market in recent years, most insurers have shifted their focus to the urban areas.
- Among those insurers, China Life has got more advantages than others in terms of more developed networks, particularly at the grass roots.
- In case of a takeover, the current MOCA/MOLSS staff have good reasons to be worried about their future because the commercial companies could not offer all of them suitable posts.
- On the other hand, the commercial companies are worried about the financial situation of the current MOCA/MOLSS schemes (both liabilities and assets), about possible further state intervention, and, above all, about profitability of the rural market.
- It would be expensive for farmers to participate in commercial insurance schemes.

2. Regulation: Toward Consumer Protection in Financial Markets

The ADB report on urban pension reform has made a strong case that sound regulation and supervision of the financial markets and services are essential to the operation of a funded pension scheme. As mentioned earlier, regulatory agencies are developing in the PRC. In September 2000 the PRC set up a National Social Security Foundation. The council of that foundation is responsible for supervising the operation of pension funds. Regulation of fund management, of financial markets, and of the stock exchange is becoming more important with increasing liberalization of fund investment. In 2001 the State Council declared allowing 15% of pension funds to be invested in shares.

Currently, the issue is more pressing for the urban scheme because funds are much larger and less transparent than in the rural schemes. If the rural scheme, in whatever form, should expand in the future, regulation would become more important.

As regards the supply side of financial markets, there is a strong move toward improving regulation. The ADB urban report also analyzes the issue in depth. In the rest of this section we focus on an aspect that has received insufficient attention in the debate. We maintain that the sound operation of financial markets for pension funds requires not only regulation of the supply side, of corporate actors, and market transactions between them, but also a regulation of the demand side, that is consumer protection. Clients need assistance and protection vis-à-vis large-scale corporations. This is the social side of regulation that ought to supplement the economic and financial side. Companies must be subjected to rules concerning the dealings with their actual and potential clients.

Consumer protection is also relevant for the urban scheme, but even more for rural schemes since generally farmers are less educated, less knowledgeable about legal rights, and have less access to advisory services that mostly operate in towns and cities.

In European countries the issue of consumer protection in this field emerged only over the last 20 years, long after markets for private provision for old age began to operate. The PRC could learn from this experience and adopt similar measures at an earlier stage. Not before long, the PRC may face social unrest when an increasing number of citizens take up commercial provisions and then some find that they have been given a bad deal by the provider or have even been cheated. Such scandals are familiar in Western countries, and they have caused considerable trouble for the government (Box 36).

**Box 36: Scandals in An Under-Regulated Private Pension Market
—The Case of Britain**

The "misselling" (false selling) scandal in the late 1980s involved unscrupulous pension salesmen persuading citizens to switch from company funds into another, inferior kind of private investment, Personal Pensions. It usually would be better to remain in a company fund, because employers pay in an extra contribution. This scandal has never been fully resolved. It became possible only when the Thatcher Government stopped companies from making membership in their company pension fund a condition of employment.

In 1991, Robert Maxwell, a former Labour Member of Parliament and head of a complex business empire, was found dead, and up to £450 million was missing from the pension funds of his companies—a huge sum.

A large amount of Mirror Group pension fund money was being invested in companies where Maxwell had an interest. His private companies accumulated huge debts. To cover these, Maxwell borrowed money from various pension schemes. He also supported the share price of his companies by using pension fund assets. Despite letters from concerned pension scheme members, no regulator took any action.

The fraud caused considerable financial and psychological distress to 16,000 pension scheme members. Under public pressure, big business from the City of London made efforts to ensure that all pension entitlements were eventually paid.

The scandal coincided with a worsening recession. In that situation, millions of workers and pensioners became fearful that unscrupulous employers might "do a Maxwell" and abuse their pension funds to make up for a shortfall in company profits.

The scandal prompted parliamentary activity. A new framework was established to ensure that funds would be safe in future. In the last resort, a compensation fund would make good any shortfall due to fraud.

The British scandals triggered a tightening of regulation. Although a liberal society, Britain installed more comprehensive and stricter regulations than a country like Germany, which has a reputation of being over-regulated.

The following are key fields of social regulation of private provision for old age.

- incentives to join a private scheme, e.g. by tax deductions; every Western country has such incentives and it is most unlikely that the PRC will be able to do without in the medium-term, even if some officials believe so; the insurance industry relies on such support;
- quality supervision of private providers;
- supervision of banking and insurance industry;
- securing the quality of marketing and sales advice by private providers;
- coordinating provision for old age with other public programs and incentives, e.g., for housing and mortgages; and
- providing basic minimum income for people who cannot sufficiently provide for themselves or in case of a crisis in the financial markets.

Germany has taken to private provisions for old age fairly late, at least on a larger scale. In June 2001 a comprehensive reform of old-age pensions was enacted, which for the first time included private provision as part of an organized public-private income mix. Having a long welfare state tradition, the introduction of private provisions is accompanied by a comprehensive social regulation designed to protect the interests of the consumers (Box 37). This could also inform the PRC debate.

**Box 37: Regulation of Private Provision for Old Age under the
New German Pensions Act (2001)**

Participation in a personal or occupational pension scheme is not mandatory. Instead, the state encourages the citizens' involvement in personal and occupational (commercial) pension schemes by granting subsidies. It is assumed, however, that the private provision only supplements the public pension that is still fairly high. The grants will be delivered as allowances to go into the personal or occupational pension plan, and/or as tax deductions.

The finance and insurance industry is keen on the profits that the new legislation will bring them. It is expected that many new products for private pension provision will be put on the market. The traditional life insurance is only one of many products. Life insurance has in fact become fairly unpopular among consumers because of low returns.

The Government plans to establish a second new federal authority to certify newly introduced products for private pension provision. Only certified products for private pension provision can be subsidized: The products will have to

- guarantee that payment of benefits will not start before benefits from a state pension scheme are paid or before the age of 60;
- guarantee monthly paid benefits until death—the monthly paid sum has to stay on the same level or increase, it must not decline;
- guarantee that at least the sum of the paid contribution is paid back (nominal value); and
- be protected against seizure.

Under special conditions, home property can also be subsidized as provision for old age.

To protect the citizens against unscrupulous product offers (consumer protection), the banks and insurance companies will be obliged to comply with some obligations concerning information and reporting. In case of noncompliance with these obligations, the company will have to pay a fine. In addition, the companies have to report on their ethical, social, and ecological considerations when investing the paid contributions.

Not only personal pension schemes but also occupational pension schemes in form of direct insurance and mutual pension funds can be subsidized.

Chapter 7. POLICY PERSPECTIVES

A. Designing Pension Schemes for the Rural PRC: Principles and Options

Based on the findings set out in the previous chapters, this section depicts five models for the designing of pensions in the rural areas. We start with summarizing general principles of institutional reform that cut across the five options.

The following principles of reform have emerged from this study.

- *Base entitlements on employment whenever there is an employer.* This principle reacts to the rural industrialization and it can be useful both for employees and employers (Chapter 6.C). Some self-employed might be included by devising ways of treating them similar to employees.
- *Make participation in the scheme compulsory, at least for designated groups.* This will make full use of the ability to pay of many persons who otherwise would not join although they could. Compulsory membership also provides a basis for pooling and redistribution. Further, it may reduce the gender bias in participation, found, e.g., in the current rural pilot schemes (Chapter 6.A). Compulsion will also reduce the need for social assistance by guiding people to take a long view of their lives and provide for themselves through contributory schemes.
- *Elements of social redistribution are inevitable.* As experienced in all European countries—rich or poor, recently or at an equally early stage as the PRC—farmers are a poorer section of society that cannot fully provide for themselves (Chapter 4.D). Pooling, state subsidies, and tax deductions for contributions to public and commercial schemes are key instruments.
- *Pension reform is more than reforming pensions.* An integrated reform of old-age security also has to think about the various need-based systems (social assistance) and merit-based systems (pensions for cadres, civil servants, and servicemen). All of them cater to the elderly and all will have to cope with the ageing of the population. Moreover, insufficient pensions increase the need for social assistance (Chapter 7.B). Morally, ageing and unemployment are problems of society at large and the ensuing burdens should not only be put on the shoulders of urban workers and farmers and their respective pension schemes.
- *Take a national view beyond the rural-urban divide.* First, the category "rural" is no longer suited as a basis of pension reform due to the rise of rural industry and migration. Many "farmers" do not work in agriculture. Second, rural and urban areas are increasingly linked, through migration and urban pension entitlements in some rural TVEs. This poses problems of compatibility of security systems and of transfer of entitlements. Third, current financial demands made by the urban pension system raise moral questions of a just distribution of resources in the PRC society. These issues go beyond the simplified question if rural and urban schemes should be unified or not.
- *Modernize the legal and administrative foundations of old-age security.* This includes creating of specialized agencies separate from enterprises and government, increasing administrative capacities, professionalizing staff, and standardizing procedures and national legislation. In this field much has already been done, with the major exception of a law on social security that would include rural citizens.

- *Take into account the needs and wishes of the clients*, that is the pensioners and the contributors. Pension reform is not only administrative reform. This includes transparency and trustworthiness of pension policy and pension schemes, a concern for special needs of special groups like the poorest and women, and advisory services and consumer protection (Chapter 7.B). Pensions are not only about money. They can also be a moral basis of national unity and undivided citizenship.

We now discuss five options that fall into two groups.

- There are three antiwelfare state options advocated or considered by central government officials and leaders: a nonpension policy (option 1), commercial provision (option 2), and a scheme linked to family planning and confined to one-child families (option 3).
- The two prowelfare state options are an extension of the current MOLSS pilot schemes (option 4, advocated, e.g., by many local administrators) and proper social insurance (option 5, deriving from European experience, but hardly figuring in the PRC debate).

The main finding of this summary section is that the three antiwelfare state options considered by the central government are seriously flawed and should not be pursued. The two prowelfare state options, by contrast, seem to be viable and morally justifiable avenues at least for better-off areas. In Chapter 8 we outline a practical plan for action in implementing the more comprehensive of the two prowelfare state options—social insurance.

These are stylized models that highlight issues of reform. They allow for a wide range of choices and institutional specification.

1. Option 1: A No-Pension Policy

The nondecision about the future of rural old-age security since 1997 amounts to a non-pension policy. It is not easy to blame politicians for nonaction when problems are difficult and views among the leadership are divided. There seems to be no immediate pressure for action since rural pensions are not linked to current economic reforms (unlike urban pensions that are linked to SOE reform) and the danger of social unrest arising from inaction is limited.

However, a nondecision is also a decision. It does not leave the future open. First, a pension scheme already exists in the countryside. The inaction by government, the lack of support, has seriously damaged the scheme (Chapters 2.B and 6.E). With every year of inaction, it will lose further ground among local administrators and participants.

Second, inaction is an implicit decision in favor of commercial schemes. It is a kind of passive commercialization, which means letting anybody take up commercial insurance or private pensions if he or she can. Government would neither care for those who cannot, nor seek to regulate the supply side of private pensions. In Chapter 6.E, we outlined the likely consequences of such strategy based on previous experience in the countryside: large coverage gaps, "creaming" the rural population, high cost, a risk for farmers of being cheated, and little interest by commercial companies due to high transaction costs and small contracts.

A nonpension policy would narrow future choices: If future leaders should want to choose public schemes they might find themselves left with the poorest clientele not covered for by commercial providers. Those who joined commercial schemes have made financial commitments for several decades and could hardly switch.

Moreover, a nonpension policy is not sustainable. Soon, needs for social assistance will rise to fill gaps of coverage and insufficient benefits. With the new Minimum Living Standard System (MLSS) these needs cannot easily be averted. Needs for regulating private pension markets will also arise. All in all, it is open to question how long the current nonpension policy can be sustained and what irreversible consequences it may entail.

2. Option 2: Commercial Provision

If politics should choose this option, several problems would have to be dealt with. Some problems have been depicted in the context of Option 1, which we analyzed as a passive kind of commercialization.

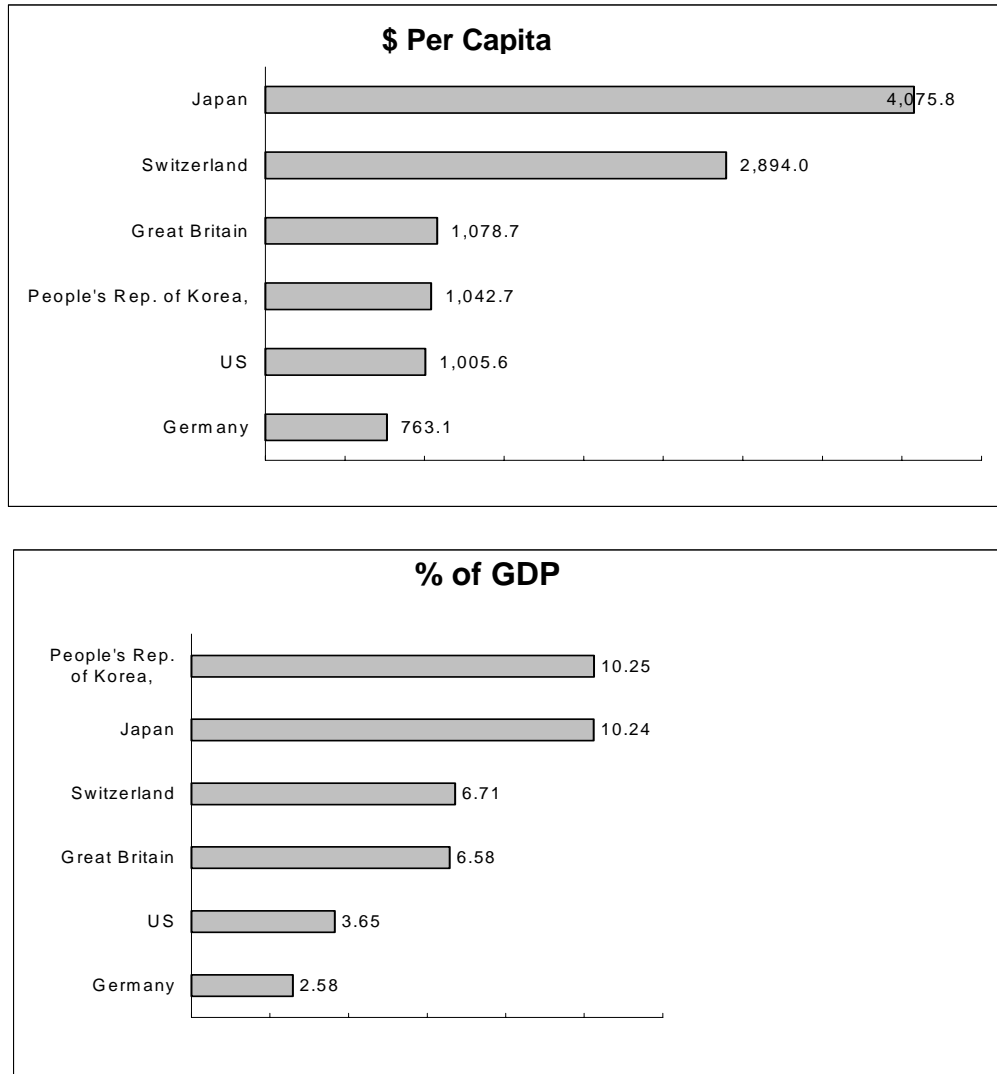
First, Government should pursue an active commercialization, i.e., creating a sound market for financial services and commercial providers by comprehensive regulation. Regulation should not only refer to corporate actors and transactions in financial markets (supply side), but also to consumer protection for those who want to take up commercial provision (demand side, Chapter 6.E). This is particularly important for farmers who tend to be less educated and have less legal knowledge. This kind of regulation also serves the overriding goal of securing social stability in the countryside. Scandals revolving around fraud and false selling of financial products have aroused considerable public uproar in Western countries (Chapter 6.E, Box 36).

Second, supplementary public schemes would be needed to care for those who have no or insufficient commercial entitlements and to compensate for a general devaluation of assets during a crisis of the financial markets. Insecurity of benefits and inequitable participation are key problems of commercial provisions. This might be a (costly) case for the MLSS. Current experience shows, however, that the MLSS cannot be financed in many rural areas. Participation in commercial schemes could also be made compulsory, though only in richer areas and with subsidies for the poorest.

Third, should the Government seek to enter a public-commercial partnership, it should resist the temptation so common in the PRC to build on a supply monopoly. However, this may be difficult to avoid since in our interviews only one of the big commercial insurers showed an interest in taking over the MOCA/MOLSS scheme (Chapter 6.E).

Fourth, the PRC debates seem to be stuck with life insurance. However, there are a variety of financial products. The Government should actively encourage widening the market. The public-private partnership introduced in the German Pension Reform Act of June 2001 (Chapter 6.E, Box 37) has kindled an explosion of new products even before it was passed by parliament. Life insurance is losing ground, e.g., in Germany, due to low returns.

The preference for life insurance may also be related to cultural differences, as suggested by the divergence between countries with regard to the share of life insurance (Figure 8). Generally, the preference for commercial provision seems to be culture-bound, depending on the historical experience of a country. In Germany, for example, assets were destroyed twice in the 20th century by war and postwar hyperinflation. This made for a preference for public pay-as-you-go (PAYG) provisions.

Figure 7: Life Insurance Contributions in Different Countries, 1995

Source: Lowe 1998.

3. Option 3: Pensions for One-Child and Two-Daughter Families

This scheme has been devised and would be run by the State Family Planning Commission (SFPC) (Chapter 2.B). It was also alluded to in Document No. 8 (2 March 2000) of the State Council. However, when detailed regulations for the implementation of the scheme were submitted to the State Council in early summer 2001, the idea was vetoed by the Prime Minister who rejects any kind of public pension for rural areas.

The scheme is quite unusual. By definition the concept is confined to a certain group. In this way it is partially a nonpension policy like Option 1. It is also questionable if it is an old-age security scheme at all or predominantly a scheme to promote family planning. Morally it is based

on merit regarding family size, and not on security in old age. These two goals do not go together easily.

Looking into the future, the scheme could be problematic. First, it would only be a transitory solution since the one-child policy will not be carried on forever. Sooner than expected the PRC may find itself in a situation like Western countries today, seeking to increase the birth rate. Pension policy is a long-term issue because it relies on trust in institutions. A new pension scheme that may have to replace this would have to generate new trust.

Second, the scheme puts a premium on a generative behavior (having only one child) that kindles the ageing of the population—the number of elderly per 100 adults of working age would further rise. This would cause problems for a PAYG system, but funded systems (this scheme is designed to be funded) would also be affected.

However, the SFPC scheme might be a pragmatic starting point that could grow into something bigger, a social insurance with wider coverage. Lin (1994) proposes a graded scheme with 100% benefits for the childless elderly, 50% for parents with one child, and 33% for parents with two children. Lin argues that under conditions of fiscal constraints, it is justifiable to give priority to the most needy—those with less support from children.

4. Option 4: Extending the MOCAMOLSS Pilot Scheme

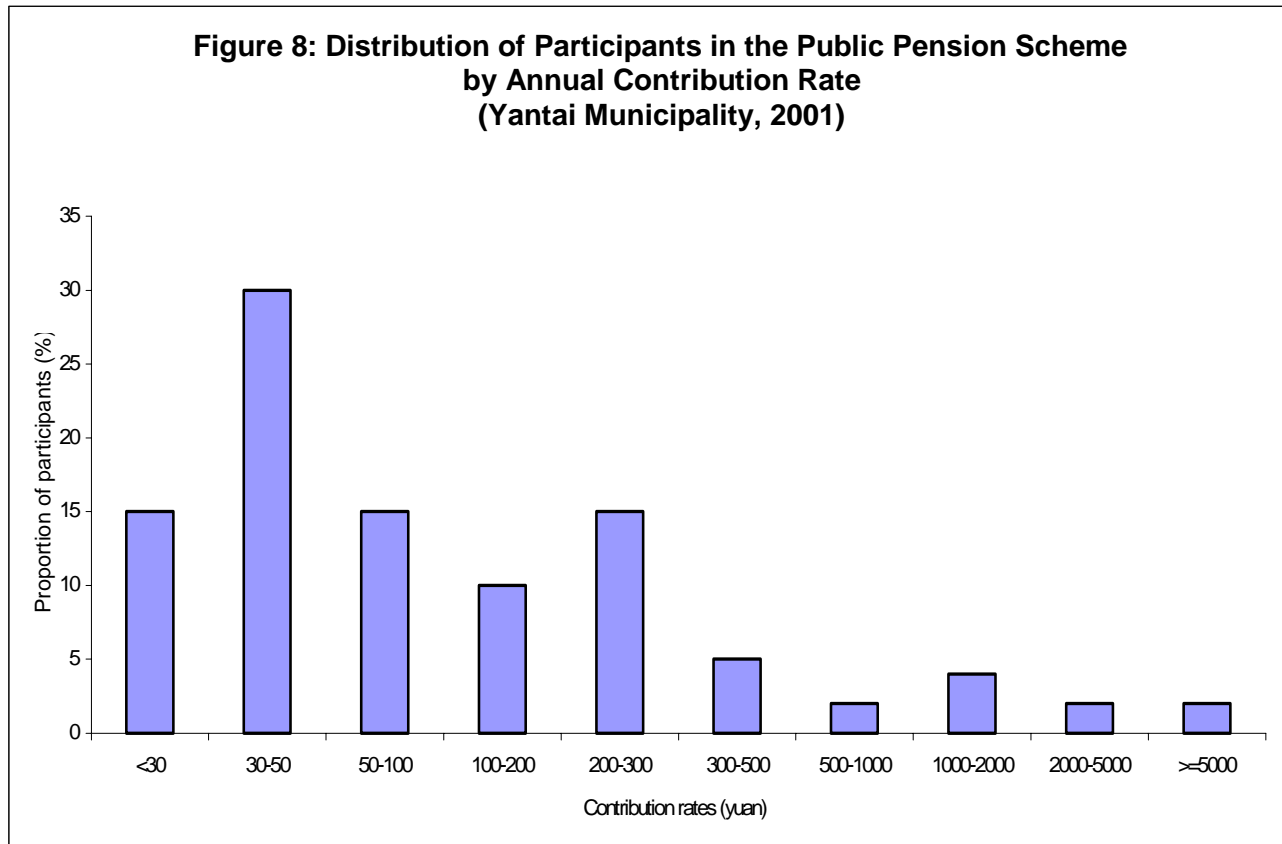
Our examination of the scheme and a previous evaluation carried out in 1995 (Chapter 6.B) concluded that it works fairly well and that popular criticism has to be seriously qualified. The problems of the scheme are not a reason to give it up. However, we also found that it is an embryonic form of pensions, with neither defined contributions nor defined benefits. Benefits can be below what would reasonably be called a pension.

It is a system of organized saving. On the one hand, this is an achievement in a developing country (Gillion 2000). On the other hand, when planning for the future, this will not do. Coverage could certainly be extended in richer areas, even beyond two thirds of the rural population, as evidenced by Yantai Municipality, Shandong. People could also pay higher contributions because nonparticipation is not only caused by inability to pay (Chapter 6.D).

But a substantial development would have to take it toward social insurance (Option 5), by introducing

- defined benefits or defined contributions,
- redistribution to replace and extend the current hidden forms of redistribution (Chapter 6.C) and
- subsidies to replace and standardize the current disorganized system of local subsidies.

In richer areas, subsidies from various levels of government are within reach of what is feasible financially. For Yantai Municipality, the local Labour and Social Security Bureau has calculated the amount needed on the basis of the comprehensive client data (for a rough picture see Figure 8): To ensure that all citizens reach a pension at or above the poverty line, 1% of the municipal budget would have to be spent on subsidies to the contributions of the poorest. The switch to urban pensions in some TVEs also raises the question of going beyond organized saving.



Source: Yantai Municipality, Labour and Social Security Bureau.

Whatever extension will be pursued, the Government support, not only in money terms, but in political terms, which is now lacking—will be an essential prerequisite for the success of the scheme. However, it may be too late now to resume the current pension design. Staff and citizens have been demotivated. They may not be mobilized by a political sign that just says "go on," especially since the development in the near future is likely to go beyond organized saving. Setting up a pension scheme is a big undertaking that requires changes in basic attitudes of citizens. The MOCA/MOLSS scheme needed years of promotion.

Today, a new departure would be needed; a new motivation, and this could be the road to social insurance. The historical experiment of rural pensions could still claim to have laid the foundation for people to acquire a long-term view of their lives.

5. Option 5: Social Insurance (in two parts)

The key characteristics of social insurance are

- compulsory participation,
- social redistribution,
- nonprofit operation, and

- an independent agency that administers contributory funds and entitlements, unlike social assistance and provisions for civil servants that are administered and financed by government.

Within this framework, social insurance offers a wide range of choices.

The rural population could not be covered by a normal social insurance scheme that treats participants basically as equals and provides benefits that account for a substantial, if not the biggest part of, income in old age. This, however, does not imply excluding the poorer sections, at least not in richer areas with a smaller number of poor people. They could be integrated into a scheme that formally extends to all citizens but is divided in two parts or segments.

The primary, employment-based segment would be closer to social insurance as found in the urban sector or in Western countries. It would cover all people in employment, i.e., in rural areas basically TVE employees. Well-off agricultural farmers could join voluntarily and be included on similar terms as the urban self-employed in the urban workers pension scheme.

The secondary, farming-based segment would be confined to real farmers who mainly earn their living through land use. This part would still have basic characteristics of social insurance, like contributions paid by participants and, to a degree, earnings-related benefits. It would not be tax-financed social assistance, but would rely on heavy subsidies from Government.

This dual structure is the model adopted by most European countries for their farming population (Chapter 4.D). Only the universalist schemes in Scandinavian countries chose a unified approach. Different versions can be found in Europe, ranging from separate schemes for farmers to separate rules for farmers within more encompassing schemes. Over time, the secondary segment could gradually adopt similar benefits.

State subsidies for the secondary segment can be justified on two grounds. First, for poor farmers small sums of money have a higher marginal return than for better-off people in more urbanized areas. A small additional income would make a difference for poor people. In the field visits we found how important small pensions were. In very poor villages both price and aspiration levels of the population are so low that sums that buy almost nothing for urban citizens would raise the standard of living for the poor. Benefits might also include free access to medical services for the elderly. This alone is likely to enhance acceptance of the scheme.

Second, there is a moral justification. TVE employees on average have a higher income and are younger. When letting them join the employment-based primary segment of the scheme (or even the urban scheme), they leave behind an older clientele with lower incomes that would have to be catered to by the secondary segment. Migration to cities, combined with membership in the urban pension scheme, has the same effect. This means that both systems—the rural employment-based segment and the urban workers scheme—regenerate their clientele with regard to age and income at the expense of the farming-based secondary segment. This should be a reason to use taxpayers' money from the whole of PRC to subsidize the modest scheme for agricultural farmers.

How to finance the dualistic model of social insurance? Both funding and the PAYG are difficult in rural areas. None is obviously superior, not to mention that much government money

would have to be put in the scheme irrespective of the mode of finance. Contributions by poor farmers will be low.

The PAYG would be more directly affected by the decreasing size and the ageing of the farming population expected to ensue from emigration to cities and, as regards the secondary segment, from moves to rural industry. It would be a demographically dying population with an increasing imbalance between the number of new contributors and the number of pensioners.

However, a PAYG system could be introduced on the spot, whereas entitlements from accumulated funds would have to be built up over decades. In that case, large parts of the rural population would be excluded from the system—unless massive one-off subsidies were paid to these people to get the funded system started. This is problem of transition to a new scheme that can never be avoided. Since some farmers have already paid into the funded MOCA/MOLSS scheme, the introduction of the PAYG would also require measures to facilitate the transition.

Moreover, younger people might be reluctant to pay into a funded scheme, expecting a switch to industry or cities in the near future. The PAYG would also have the advantage of the benefits being seen at once, in the form of pensions received by the parents of the contributors, while the growth of accumulated capital is rather abstract.

For the general design of the social insurance scheme, the broad range of models found in advanced Western welfare states can serve as inspiration. The view should not be restricted to countries like Chile or Uruguay as recommended by some experts. Again, setting up pension schemes is planning for the future. In 20 or 30 years time the PRC may be more similar to present-day advanced countries than to developing or transitional countries.

B. Supporting Benefits and Services

Pension policy is more than organizing the transfer of cash to a bank account. In this section we look at social benefits and services outside the field of pension that could and should support pensions.

Medical services and education impact on pension schemes since citizens have to pay for both (Chapter 6.D). Medical impoverishment also affects the elderly. For the middle aged, medical and schooling expenses considerably restrict their ability to pay contributions to pension scheme. Making health and education freely available at least for poorer people would make it much easier for pension systems to operate. Support by nongovernment organizations (NGOs), e.g. the HOPE project for the education of children, would also be helpful.

Pensions are a cash benefit, and discussions tend to center on questions of finance. However, especially for farmers, supporting advisory services and counseling would be helpful. Germany could be a model (Chapter 4.D, Boxes 7 and 8). There is an extended network of advice centers for farmers run by Government, farmers associations, and NGOs. Besides advice on pensions, general advice is given on retirement, e.g., handing over the farm to a son, on claiming public benefits, on farming, on psychological problems typical for rural households, etc.

In the PRC such advice could help farmers find their way in a rapidly changing society, e.g., whether they should switch to a TVE, how to combine TVE and farming, or how to provide for ill health and accidents. With regard to commercial insurance for various contingencies,

advice is also much needed. This would be a form of consumer protection (Chapter 6.E). Fake products, e.g., fake fertilizers, are a major concern in rural areas (Liu 1999). Withholding due wages by employers is equally a problem in towns (Chapter 6.C, Box 24). Protection against buying a fake or fraudulent insurance is another area where legal protection is needed.

Advice centers for pensioners can draw on precedents. The National Committee on Ageing already provides consultant services for the elderly and also helps set up elderly associations in rural areas. The Roman Catholic NGO Misereor helps to set up legal advice centers. There is also a network of advice centers for people with disabilities.

Another supporting measure would be social reporting and monitoring in the field of pensions and the living situation of the elderly. There is already much research by various PRC agencies on the problems of the elderly. Social reporting and monitoring, by contrast, is an instrument of social planning. It means

- choosing social indicators to measure the living conditions of the elderly, including indicators of subjective well-being, in a standardized way;
- defining standards or thresholds for these indicators to assess who falls; and
- collecting related data regularly (normally annually) to trace the changes in society.

The claim that family support and land use provide for old age in the rural PRC, for example, can be tested by social indicators. Changes in the support capacity of these forms of support will be reflected in changes in the indicators. Another example, taken from Germany, is an annual report on the state of old-age pensions. Social reporting and monitoring could be organized by a special advisory board of experts on social policy questions.

1. The Minimum Living Standard System

The last type of measure to support pensions is of a different kind: social assistance. It is relevant to pensions in three ways.

- The traditional forms of social assistance in the PRC at the village level—Five Guarantees, Poor Relief, Disaster Relief—also cater to the elderly, the Five Guarantees scheme even almost exclusively. From 1996 the Minimum Living Standard System (MLSS) has been extended to some rural areas, and many of its beneficiaries are old people. For many elderly, probably for most, social assistance is the only benefit they get.
- Social assistance may also be paid to recipients of pensions when pensions are too low. In all Western welfare states some kind of social assistance is provided to supplement social insurance.
- Developed forms of social assistance like the MLSS could also be conceived as the main provision for old age, as an alternative to pensions. A special social assistance scheme with flat-rate benefits was announced in 1995 by the Indian Government (Chapter 4.C).

Like the introduction of pilot pension schemes since 1991, the introduction of the MLSS is a major departure in social policy, a step toward a modern welfare state. It is unique in developing countries where poor relief is not normally administered on a formal and centralized basis; like the rural pensions, the rural MLSS originated in Yantai Municipality; and it is also still in an embryonic stage, marking a first step into a new direction. The MLSS displays several features of a modern system of social assistance.

- A formal and centralized administration reduces the amount of discretion and arbitrariness typical of traditional poor relief and local charity. Still, as in Western countries, there remains scope for local specification and individual discretion.
- A precise minimum living standard is defined, an income threshold that marks the point of intervention by the social administration. It is a universal system, not a categorical one like the Five Guarantees that requires the Three No's as condition of eligibility.
- It also caters to permanent need, not only, as the traditional forms of social assistance at the village level, to temporary situations of need.
- Benefits may include payments for special purposes beyond subsistence, especially for the education of children and for health. In Yantai Municipality, for instance, 30% of high health expenditure may be taken by the MLSS. In this way a comprehensive minimum standard is established.
- Social scientific instruments are used to develop the system. In Yantai Municipality a household survey was conducted to explore the income and the expenditure of rural households.

The rural MLSS differs from the urban one in three respects. First, it was introduced three years later. Second, the minimum living standard, the income threshold, is set far below the poverty line whereas in urban areas the poverty line also marks the minimum living standard. This means that the scheme is not fully need-oriented. In Yantai Municipality the threshold is defined by almost one third of living expenditure (1,980 yuan), that is 600 yuan per year in Zhaoyuan City. In Muping County in the same municipality, the level is 580 yuan per year. Third, there are considerable difficulties in setting up the schemes in poor areas while the urban scheme is being extended nationwide.

At the moment there are three main problems in developing the MLSS in rural areas.

- How to define the standard? Although social scientific investigations are sometimes used, fiscal considerations rather than actual cost of living seem to determine the level of the minimum standard in the last resort, for example, in Hubei Province.
- How to measure income? In urban areas where money income prevails (wages) this is less of a problem. But in rural areas with a less monetized economy and much of farmers' activity going into production for subsistence and mutual aid, it is more difficult to assess the income of an applicant to identify his real needs.
- Finance: Poor areas cannot afford the scheme.

In richer areas obviously the scheme can be run more easily. In Yantai Municipality, finance is shared by the counties (30%), the townships (30%), and the villages (40%). Originally the municipality should also have contributed but the counties in Yantai were deemed rich enough to do without. This multilevel way of financing goes beyond the more localized financing of social assistance in many developed countries.

The financial problems become apparent in Yunnan and Hubei. In Yunnan there is an urban MLSS but no rural one. For rural areas it is not even planned, with the possible exception of some richer areas. Even to secure a low standard, money does not suffice, as revealed by the officials at the provincial level. Officials at the county level (Wuding County) even referred to the problem of moral hazard—the farmers becoming lazy through benefits—though this problem may seem remote under such circumstances. Even the urban scheme provides very low level of benefits: for instance in Kunming the minimum living standard is set at 270 yuan per month, in Chuoxiong Prefecture 170 yuan, and in Dali 104 yuan.

In Hubei Province, the scheme was soon stopped for financial reasons. It started in August 1997 only to be discontinued in March 1999. The level was 50 yuan per month, much below the urban level (143 yuan per month); and the poverty line (900 Y per year). It amounted to less than a quarter of average income.

If the MLSS should be developed further while old age pensions linger unreformed, the MLSS might turn into a quasi-pension for the rural elderly.

C. A National Scheme?

The discussion of policy principles and options in Chapter 7.A left open the question of a separate system for rural areas should be established or a unified national scheme. In this section we argue that this question is secondary to the question of which principles the two systems should be based on and how they should or could be linked. Depending on the arrangement this might still be called a national system. Unification in this view is only one form of coordinating rural and urban pensions.

There three reasons for a national or nationally coordinated scheme.

- Labor mobility: Migration to cities is a major factor of economic development. Labor mobility is a crucial requisite of a fullyfledged labor market. Migration within rural areas currently poses no problems. Entitlements under the rural pilot schemes travel well from one village to another. Also, if migrants return to their home villages, they can claim the pension that ensues from previous contributions. However, if they want to pull out, they only get their own contributions back, not the village subsidy.
- As explained earlier, the categories rural and urban have become useless as a basis for setting up pension systems (or any other institution). TVE and, again, migrants cut across this distinction. Therefore an overarching approach is required.
- Equity: The original social contract made at the time of liberation was that farmers get land through land reform while the urban workers get generous social security provisions (Chapter 2.A). It can be argued that things have changed since: that land (and family support) is weakened as support in old age and that the rural-urban income gap has widened. Moreover, many "farmers" nowadays do similar jobs as their urban counterparts but only participate in an inferior pension scheme, if any.

Indeed the rural system is inferior in many ways. Benefits are normally much less generous, there is no large-scale subsidy by central Government and no or (in case of some TVE) little equivalent to employers' contributions and, above all, there is little political support by Government. Unlike the current situation in the urban reform, farmers do not expect that Government would step in if the rural system were in trouble.

Moreover, the rural system has not created the notion of retirement, which is essential to modern old-age security. While urban workers retire at the age of 60 or 55 (for women), and often earlier in case of hard work (55/50 years) or other forms of early retirement, farmers toil till 70 or, in very poor areas, till they die or are entirely incapacitated. In the rural system there is a pensionable age but its social significance for the elderly cannot compare with the urban age threshold. Other thresholds like the one for reducing local fees tend to exceed 60, in a national poverty county it is even 80 (Chapter 5, Table 14).

There are basically four models of national coordination.

- Unification: This is no option, at least not in the foreseeable future, because the systems differ too much. One is a small organized saving scheme, the other a generous social insurance. Moreover, the urban system is in disarray, with serious flaws both in design and operation as analyzed in the urban report. Major repairs are needed. It will be difficult enough to do these repairs. Integrating the rural scheme at the same time may be asking too much.
- However, TVE employees could be taken onboard by the urban scheme. Some TVEs have already chosen this option. The idea also figures in the political debate. Officials from the Labour and Social Security Departments in Yunnan and Hubei defined this even as an issue of rights: The TVE workers should be entitled to switching even if their employers do not want it.
- Following some European examples (Chapter 4.D), farmers could be included in an encompassing scheme but be subjected to special regulations with reduced entitlements.
- The systems could remain separate but build up similar structures with a view toward convergence over time. The German systems for blue-collar workers (founded in 1891) and for white-collar workers (founded in 1911) could serve as examples. The white-collar scheme started out with much superior entitlements but the labor movements, over decades of struggle, finally reached convergence after the second world war, although the two are still formally separate. A rural scheme built on similar principles as the urban one, even if less generous, would signal to the farmers that they are not left out, that they belong to the same nation.

The last two models would also include the TVE employees in the urban scheme, thus matching the model of social insurance with two parts presented as option no. 5 in Chapter 7.A. (This option, which assigns the real, agricultural farmers to a separate segment of the system, leaves open whether it extends to rural areas only or across the nation, as discussed here.)

After discounting the unrealistic model of unification, three models are left. In all of them, the rural and the urban segments would have to be linked. This involves three problems of coordination.

First, individual entitlements must be made transferable between the two segments to allow for labor mobility. Under a simple scheme similar to bank accounts, this is less problematic although, as mentioned, paying back previous subsidies is a problem. The more social insurance-like the systems, the more difficult it becomes. For example, when special entitlements like minimum pensions require a certain number of years of paying contributions. Social policy at the level of the European Union (EU) actually started with the problem of transfers that still keeps EU administrators and lawyers busy.

Second, there is a need for subsidizing the poorer segment of the system, by state subsidies and/or by redistribution among the members of the entire (two-segment) system through pooling of funds. In this way, social insurance in the poorer Eastern part of Germany, both for health and old age, has been subsidized by hundreds of billions deutschmark over the last 10 years.

Third, the two segments are interdependent with regard to sustainability. As mentioned earlier, the inclusion of TVE employees and migration to cities will strengthen the employment-

based segment while weakening the farming-based segment. This could be a further moral justification for state subsidies or redistribution through pooling. Criteria and procedures would have to be designed to implement such redistribution.

A new, challenging facet of the interdependence of rural and urban pensions with regard to sustainability has come to the fore in the most recent move toward rescuing the urban system by selling state assets. The ADB report on urban pensions makes a strong point of this. Colossal sums of money would become available through the sale of state-owned enterprises (SOEs) to be organized by the Social Security Fund (SSF), which was set up in September 2000. The report also mentions the additional relief of the urban system through immigration from the countryside. In the following paragraphs we aim to show that the use of proceeds from state assets sales raises questions of equity with regard to the rural system.

The argument goes that the Government has a moral obligation to secure the pensions of the urban workers that are currently at risk. The use of sales proceeds shall serve that purpose, but there are good reasons to question the equity of this approach.

First, is the obligation to maintain generous pension levels and a low age of retirement for urban workers superior to the obligation to care for elderly farmers many of whom live close to physical survival? Is it not rather a question of power, a reluctance on the side of the privileged urban SOE workers, to trim down their social entitlements (Bo 1999)?

Second, the implicit pension debt of the urban system to be repaid by state assets is a matter of definition. The urban report makes it very clear that the urban system is funded only in theory. In fact, its accounts are notional. If it is notional or PAYG, then the notion of an implicit pension debt is not applicable. Even if the ratio of contributors to pensioners might deteriorate in the future, a PAYG system offers ways to handle the imbalance, as done for the German PAYG scheme in the Reform Act of June 2001 in preparation for a much stronger ageing of the population than in the PRC. This means that the sale of state assets actually finances the transition to a new system, from PAYG to funding. Is the goal of introducing a new pension system morally superior to the alternative use of that money for rural pensions? The rural scheme is not in trouble due to overgenerosity and mishandling of funds but due to the poverty of its participants.

Third, what about state-owned land? The SOEs are worth 8,000 billion yuan. But the state-owned land is worth 25,000 billion yuan (China Daily, 4 June 2001). The question of using money from the sale of land for rural pensions has not been raised by politicians.

D. Conclusion: Is There a Case for Public Pensions in the Rural PRC? From Land Reform to Globalization

In 1991, the PRC embarked on a bold enterprise unprecedented in developing countries: setting up a formal pension scheme in the countryside. After a promising start, the scheme found itself in the doldrums by the end of the 1990s. While the much older urban workers pension scheme is in the center of government activity, triggered by the need to reform the SOEs, a decision about the future of the rural scheme is pending. The 1990s also saw another departure unprecedented in developing countries; the introduction of the Minimum Living Standard System, a step toward modern social assistance.

The PRC social security system is geared for change. Welfare states tend to be path-dependent: early decisions about institutional structures define future reform corridors. Through its generous system for urban workers, which was already established in 1951, and the provisions for cadres, civil servants, and servicemen, the PRC has in fact become a kind of welfare state. A path is already set for the majority of its population; for the rural citizens, however, there is the historical chance to define a new path.

Is there a case for old-age pensions for the rural PRC? Many people argue no, saying that it is too early and too risky (too expensive), that the traditional support systems for the elderly, family, and land, are sufficient, and that the pilot schemes initiated by the Ministry of Civil Affairs in 1991 have failed. This report, based on existing research and field visits in rich and poor counties, could refute or at least qualify most of these objections: It is not too early judged by the experience of European countries, many of which introduced pensions for farmers at similarly low or even much lower levels of economic development than PRC now. The traditional support systems still do a job but they are increasingly weakened. The industrialization and modernization of the countryside is reducing the role of land in the rural economy and in the life plans of the rural citizens. The pilot pension schemes have successfully introduced the idea of organized individual provision for old age, though in the simple form of organized saving with low benefits and a limited number of participants.

So there is little that could be brought against a full introduction of pensions in the rural PRC. However, in the absence of economic pressure (like SOE reform for urban pensions) and of rural unrest, there seems to be no positive case for pensions either.

There are several positive functions of pensions beyond the immediate goal of supporting the elderly: Pensions help reduce poverty, support family planning, educate farmers to plan their lives in the long term, and also enhance justice and social stability. All of these aims played a role when the pilot schemes were introduced, e.g., one reason was to give ordinary farmers what local cadres were acquiring in the 1970s and 1980s. It has largely gone unnoticed that pensions also became useful for rural industry as a new instrument to attract workers by offering subsidies. But the absence of a major economic rationale may account for the persistent disinterest of the central leadership in farmers pensions.

The land reform implemented by the Chinese Communist Party in the wake of the liberation gave the land to the farmers as a secure basis of living. This was a historical achievement (World Bank 1997). But today, half a century later, the use of land as a social security system for farmers limits the commercialization of the PRC agriculture. When economic globalization puts agricultural commercialization on the agenda of government, e.g., through the PRC's entry into the World Trade Organization, the introduction of old-age security will be as important for agricultural commercialization as urban pension reform is now for the commercialization of urban enterprises. In European countries, old-age security for farmers has acted as a major force of accelerating the transformation and reduction of agriculture, by facilitating a more productive land use by the younger generation and by absorbing rural surplus labor. This need could arise in China in the near future.

Beyond economic utility, social security can also be, and has been in Western countries, a part of nationbuilding. Even if the PRC Government decides not to install yet a full-fledged pension scheme in rural areas, it could create a basic framework that may grow over the years. This would signal to the farmers that they are not left out. It would be a step toward overcoming the division of citizenship that has been characteristic for communist China for five decades.

In the interviews with government officials, even among those sympathetic to public welfare provisions, we often met with a reservation toward the idea of a welfare state. A strong wave of neoliberalism is also felt in the country. This may be another reason why rural pension reform is stuck. However, it is difficult to see why the PRC should not be called a welfare state. In the urban sector at least, the rejection of state socialism has not led to a rejection of generous social security systems.

The fear that rural pensions may be risky is not unwarranted. In all Western welfare states, public provisions, once established, have shown a tendency to grow and to absorb more and more state revenue (or contributions from wages). However, no country—not even the US, if on a lower level—have escaped this momentum. At present Western welfare states are being restructured but it would be a misconception to think that the welfare state is retreating. The PRC could give up its reluctance to think of itself as a welfare state.

Chapter 8. A PLAN FOR ACTION: FILLING THE SOCIAL SECURITY GAP FOR THE RURAL ELDERLY

In this Chapter we turn the findings of the previous chapters into a practical plan of reform. In section A we provide a concise summary of the problems of rural old-age security that any reform has to face. We then propose a model of public provision for the elderly that varies by the economic status of an area (rich, middle, poor). For rich areas the key element is modern social insurance, that is, we recommend a public solution. Commercial insurance would have to solve the same problems as a public scheme and would have to provide alternative solutions for each of them. In section B we delineate practical steps for starting pension reform.

A. Problems and a Solution

Figure 9 summarizes the problems of old-age security in the rural PRC.

The key finding is that there is an institutional vacuum: The traditional arrangements for old age—family support and land use—are increasingly outlived. At the same time, new structures like the MOLSS pilot schemes and commercial insurance are little developed as yet. This creates a gap between eroding traditional arrangement for old age and underdeveloped modern ones. In rural old-age security, the PRC is in a period of transition. However, is this a problem? Some say that there is no need for formal old-age security in the rural PRC. In this view the current situation does not seem to pose any problems. However, when saying that it is "too early" to introduce pensions in the rural PRC, it is implied that in the future there may be a need for pensions. In this sense there seems to be a general consensus that the rural PRC needs public pensions even if there is disagreement about the right timing.

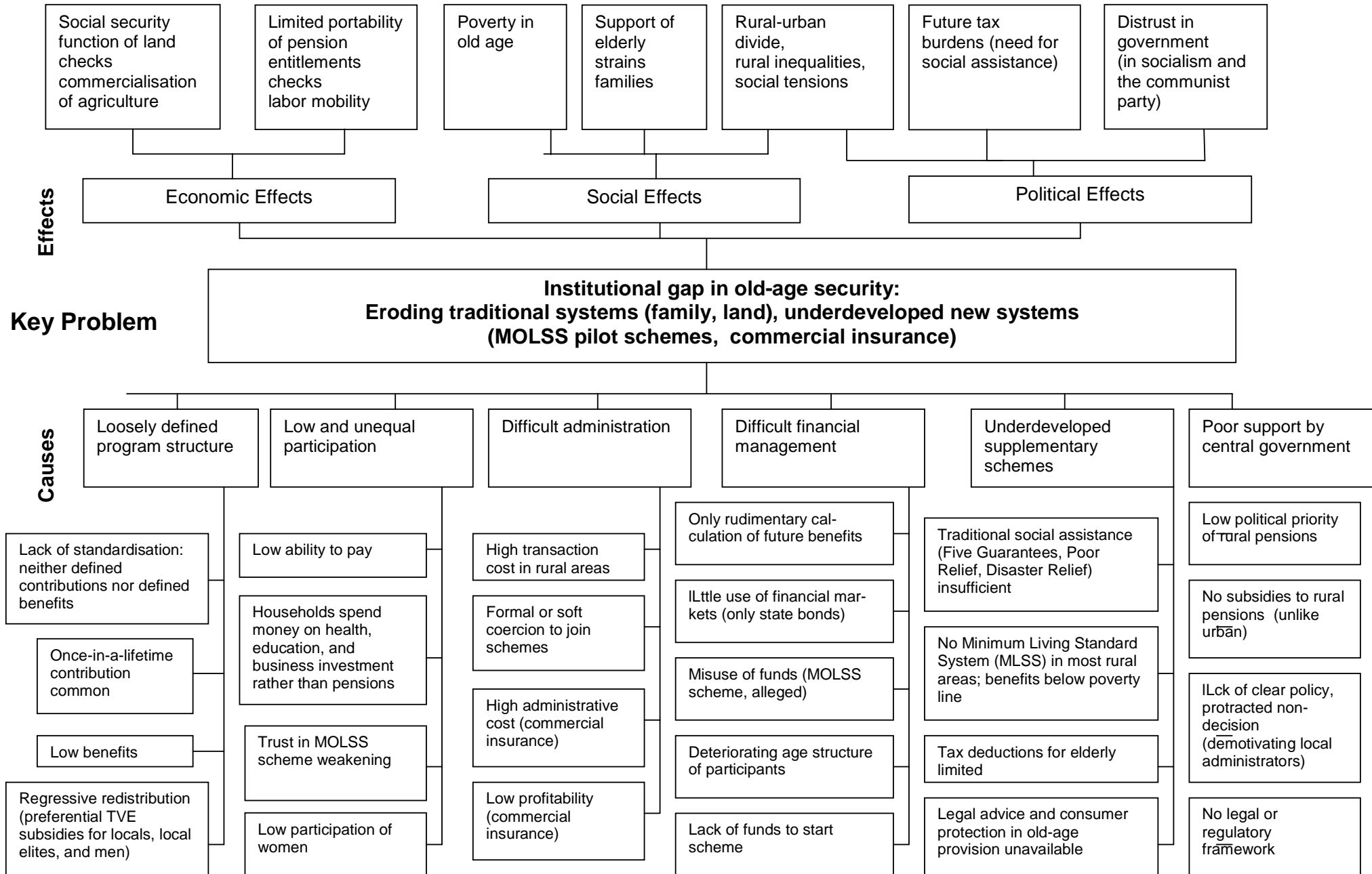
In this report we have argued that in the near future social changes in the countryside will put the issue of pensions on the political agenda. A pension system can be introduced step by step but it is important to start now. Pensions are about people's futures and a pension act would signal a commitment by Government giving citizens a perspective.

The main finding of the report is that there is a case for public pensions in the rural PRC: Pensions are both needed and possible. However, the huge economic differences between different areas must be taken into account. Individual and public resources as well as administrative infrastructure vary greatly between different provinces, municipalities, and counties. It therefore makes sense to differentiate the structure of old-age security by the economic status of the area (rich, middle, poor), by setting up different models for different areas.

Figure 10 outlines three models of old-age security: one for poor areas, another for middle areas, and yet another for rich areas. For poor areas we propose to do without any specific old-age pension but rather to rely on traditional antipoverty policies. However, we propose additional supplementary measures beyond income maintenance that are affordable by local governments and symbolize a commitment of government to the citizens concerned. For the middle areas we propose spreading the urban MLSS to rural areas on top of the measures proposed for poor areas. Only for rich areas do we propose a full-fledged social insurance of a modern kind. The details of this kind of social insurance are outlined in Figure 11.

Figures 10 and 11 give only the details of public schemes and measures. However, benefits from public sources will only be part of a wider welfare mix. Family support and land use for subsistence will still have to play a significant role supplementing public pensions.

Figure 9: Problem Tree—Rural Pension Reform



However, the character of these traditional sources will change. The strain put on children to support their parents will be reduced and social relationships among the family and kin will be less burdened by economic pressures.

Moreover, better-off people will take up commercial insurance on top of the public scheme, so they will have two layers of provision for old age. In Chapter 6.E we have argued that commercial insurance is not entirely "commercial" or "private." Most of the problems delineated in Figure 9 also apply to commercial insurance, so that a sound social policy for the elderly implies a thorough regulation of commercial insurance. In sections Chapters 6.E and 7.A we called this "active commercialisation" in contrast to "passive commercialisation."

Figure 10: A Plan for Rural Old-Age Security: Different Models for Different Areas

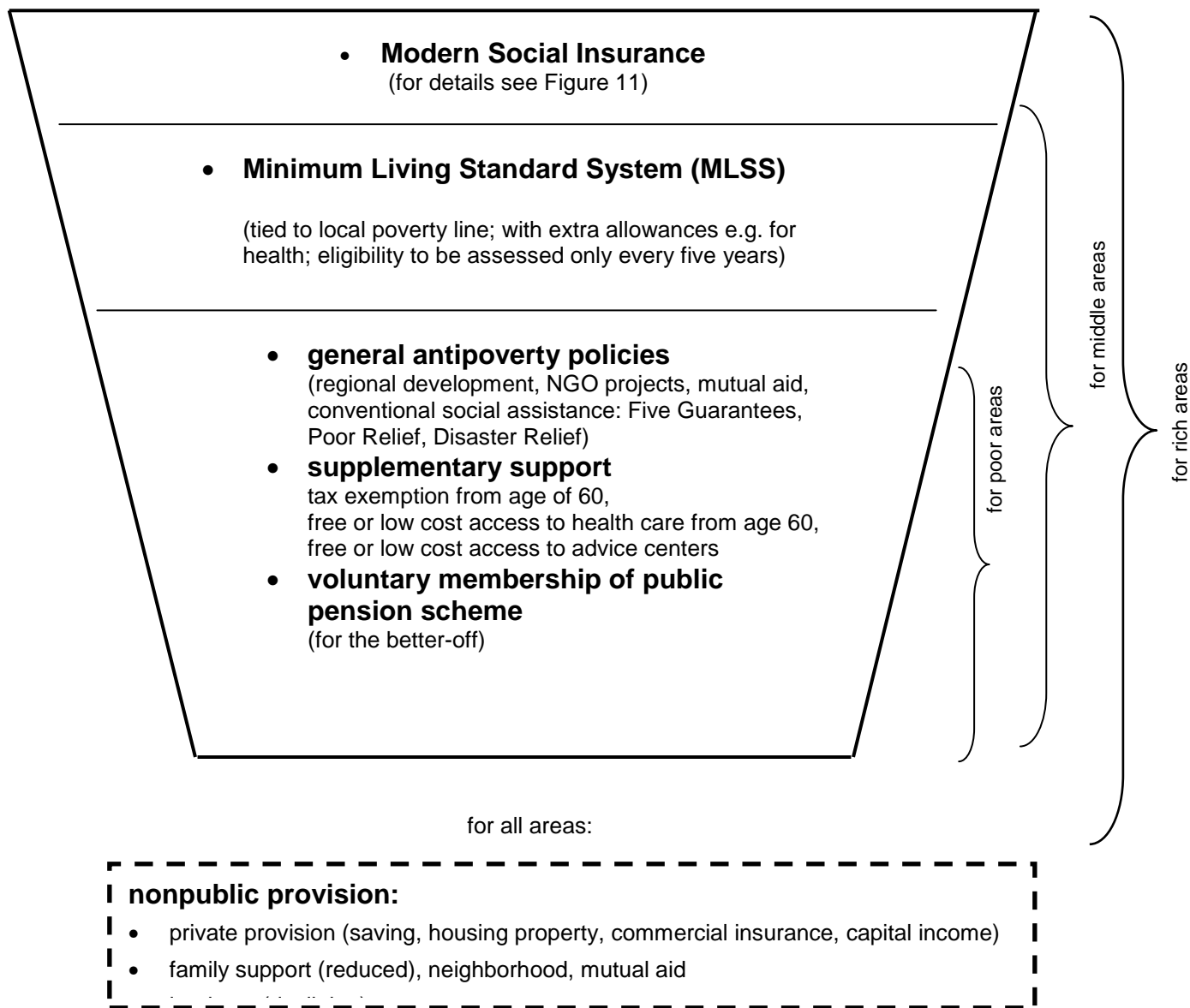
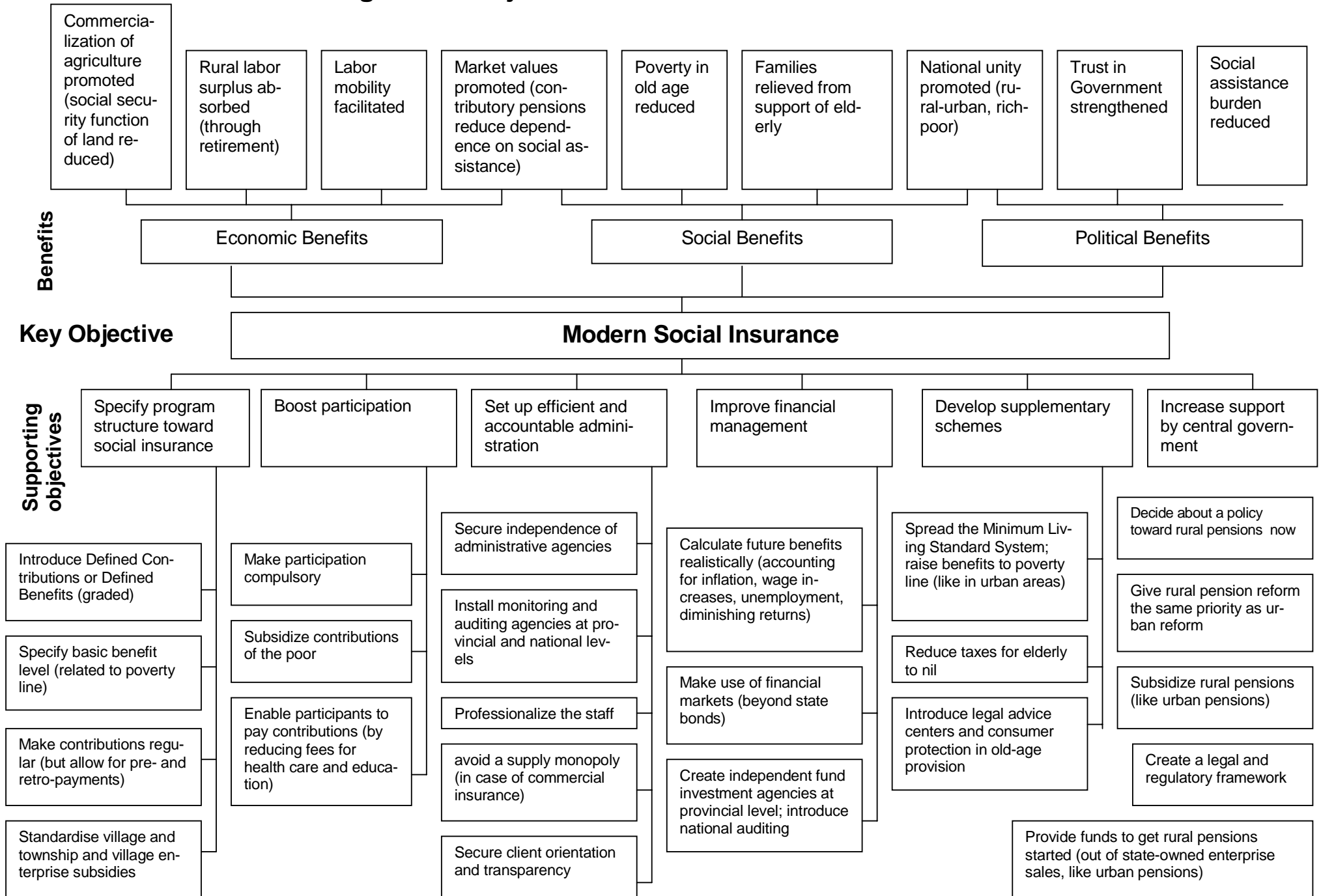


Figure 11: Objective Tree—Pension Models for Rich Areas



B. Practical Steps

1. Timing: Introduce Old-Age Pensions Stepwise but Pass a Law Now

The report has strongly argued that a decision by central Government is overdue. The protracted nondecision has been creating policy-induced problems like demotivation of local administrators and citizens.

No further pilot schemes should be started and the existing pilot schemes should lose their pilot character (i.e., they should be taken up and developed or be given up altogether). Experimental policy that draws on pilot schemes is a sound way of exploring new possibilities of policy making. However, in the field of old-age security, 10 years of experimenting is too long. Pension schemes rely on trust that has to build up over longer period. If people decide to participate in a scheme, they enter long-term financial commitments that are linked to their overall life planning. Pension policy, therefore, is less suited for experimental policy than other areas of policy making.

The immediate and first aim, therefore, is to draft and pass a law as soon as possible and to set up the necessary agencies mentioned in Figure 11. To decide and legislate now does not mean to install the whole scheme in one go. A decision is itself a piece of policy making: it symbolizes the commitment of government to the cause of old-age security for its rural citizens. The old-age pensions act to be passed may provide for a stepwise introduction of several components of the scheme.

- The law may become effective only in the future. This was done, e.g., in Germany when a great pension reform act was passed in 1989 only to become effective from 1992.
- Since we propose provisions for old age differentiated by three economic levels of areas, some areas may start at the lower end and reach the middle or top status of a full-fledged system of old-age security only later.
- The key measure for middle areas—the development of the MLSS—can be introduced stepwise. For example the level of benefits that is currently below the local poverty line (unlike the urban MLSS) may be raised gradually to reach the poverty line.
- The subsidies needed for poor participants of formal pension schemes may be built up gradually to enable local governments to adjust their budgets to the situation. Subsidies for certain groups whose economic situation might improve in the future can also be phased out within a given time span. This was enacted, for example, in the recent pension reform in Korea, which provides for subsidies to farmers' contributions to be phased out till 2006.
- Similarly, subsidies paid by central Government to get the rural system started (see section 4 below) or compensation payments from the urban pension scheme to the rural one could also be designed in a way as to be gradually reduced over the years.

2. Categorize Areas According to Economic and Administrative Levels

The first task is to decide which administrative unit should be taken as level of reference for defining rich, middle, and poor areas. To facilitate labor mobility and to secure a stable and accountable administration, a higher level of government, either province or municipality, should be chosen.

The second decision would be to decide about which province or municipality falls under which category – rich, middle, or poor. This decision should be taken jointly with the local

governments concerned. As mentioned earlier, such decision must be open to revision. Areas can be upgraded or, if necessary, downgraded.

The rich areas would primarily include the coastal areas in the East, as described in Chapter 6.D. For Yantai Municipality, Shandong, we could show that the MOLSS pilot schemes are a sound base to build on. In even richer areas like Shanghai and Southern Jiangsu, developed systems of old-age security—even a kind of local welfare state—have been established as analyzed in recent studies by Peng Xizhe and Athar Hussain.

3. Make Institutional Choices

There are no "best" solutions: Choices between different reasonable solutions must be made. No solution will be perfect. In developing countries and in rural areas, in particular, conditions for social security are difficult (Chapters 4.A and 4.B). Some of the related problems cannot be solved entirely, especially reliability and accountability of administration and financial management. Thinking in great alternatives like state versus private or public versus commercial or, for that matter, funded pensions versus PAYG are not very helpful (Chapter 3.A). In fact most of the problems named in Figure 11 apply to both, and most of the remedies outlined in figure 8.3 are needed for all types of systems to operate soundly. The following are key areas of choice.

a. Public versus Commercial

Commercial provisions are riddled with problems (Chapters 6.E and 7.A). We have argued that if commercial provision should be the main solution then a strategy of active rather than passive commercialization would be needed, i.e., a diverse range of measures undertaken by Government to regulate and frame commercial provision. That is, "going commercial" produces demands for Government, too. Commercial provision is subject to similar problems as public provision.

- Participation has to be made compulsory to reduce future social assistance burdens on government budgets. Especially with the spread of the MLSS poverty among the elderly due to insufficient pensions will increasingly lead to claims for social assistance. Moreover, as shown in Chapter 6.C, compulsory participation can also help avoid the exclusion of women from pension schemes.
- The MOLSS pension scheme has been alleged to coerce some citizens into the scheme. However, in the case of commercial insurance, it is the job of numerous sales agents who visit citizens in their homes to persuade them to contract an insurance that they otherwise would not contract. This is a kind of soft coercion.
- A bad public scheme can disappoint people and erode the trust in government. As shown in Chapter 6.E, however, cheating or selling unequitable insurance contracts to farmers can also lead to scandals and criticism of government.
- Problems of bad management and misuse of funds are ubiquitous in the PRC. Bad management cannot be used as an argument against public pensions as such. In the PRC, most public and commercial institutions are weak and are liable to mismanagement and corruption. Compared with the urban public pension scheme, where all accumulated funds have been lost the MOLSS rural schemes, are in fairly good state.
- While public schemes are criticized for offering no alternatives, in the PRC it is very likely that in the case of commercial provision in the countryside a monopoly will be established.

- Returns of invested funds may be equally insecure under commercial schemes as under private ones.

b. Funded Systems versus the PAYG

The PAYG funding seems to be a lost cause in the PRC. This could be due to the fact that a really independent social security agency and fund investment is not conceivable in the PRC at the moment. The idea of PAYG rests on the existence of a separate institution that is in charge of administering a separate budget for contributions and benefits. PAYG is not, as often assumed in the PRC, the same as the old socialist practice of paying pensions out of the general budget (of an enterprise or a local government) to meet current needs. Rather, it is a kind of collective self-provision, organized in an independent non-state agency.

Funded systems have, among others, two problems.

- Unlike the PAYG, the profit of the system is only visible to participants some 30 or 40 years later, whereas the PAYG immediately relieves the children of much of their support duties toward their parents, because their parents' pension is paid out of the contributions of the current working generation.
- Getting a funded system started is always a problem. To avoid years of a coverage gap, an external subsidy is needed. By contrast, the PAYG can start any time without subsidy.

c. Tax Deductions

Tax deductions or exemptions that are part of a strategy of improving old-age security (Figures 10 and 11) are feasible. Various agricultural taxes account for 2.5% of government revenue. Roughly calculating, a tax exemption for the elderly above 60 years of age (10% of the population) would amount to 0.25% of government revenue. A tax reduction would also be morally justifiable because urban pensions are not subject to taxation while for farmers land acts as social security, i.e. it is the equivalent of the urban pension.

d. Redistribution

We argued that, as in all European countries (Chapter 4.D), massive redistribution is needed for rural pension schemes. For richer areas a subsidy to the contributions paid by the poor would be feasible. Calculations of Yantai Municipality made for this report show that only 1% of the budget of the municipality would be required to subsidize contributions so that no citizen would fall below the poverty line in old age.

e. Benefit Standards

It is important to make choices about the level of basic benefits. In the PRC debate there seems to be a kind of consensus that benefits in rural areas must be low, according to the low economic capacity. Increasingly, the term basic security is used in this context. However, even if benefits are low it is crucial to define standards. Standards may be based on a basket of goods considered to be essential for living or be defined in some other way. Standards are not objectively given. They are a matter of value decisions about what a society owes its poorest members.

Defining standards requires a commitment by Government to certain goals. Standards also enable politicians and citizens to monitor the development of social security systems. They

can act as a yardstick. They can also be lifted with further economic growth. Defining basic benefits need not imply to restrict benefits to this baseline. Earnings-related benefits may come on top.

f. Coordination of Rural and Urban Schemes

Again, there is no one best solution—either full separation or full integration of rural and urban schemes—but a range of choices. In European countries all kinds of solution can be found: separate rural pensions, integration of farmers into more general pension schemes, and inclusion of farmers into a universal scheme that covers the entire population. We have argued in Chapter 7.C that the formal nature of the integration of rural and urban systems is second to the question how well coordinated rural and public pensions are.

The portability of pensions would be enhanced through sound coordination. In this respect the PRC can learn from the European Union (EU) because the transfer of pension entitlements between European countries is a longstanding field of social legislation of the EU. If different systems are well coordinated, then inclusion of TVE employees in urban pension systems could be an option.

4. Provide Funds to Get the Rural Pension System Started—The Problem of Transition

Irrespective of system design, the transition to a new pension system always poses problems. This can be seen in the current reform of the urban pension scheme: A massive injection of money from selling of SOEs is planned to start the urban system anew as a funded system (because previous funds have been lost, turning it into a PAYG system in actual fact). From this source pensions could be paid at once to the present-day elderly. In this way the profits of the new system will be made visible at once and acceptance would be enhanced.

Morally it would be justifiable to use part of the proceeds of the SOE sales also for rural pensions. There is no reason why the total loss of the urban pension funds should be compensated out of national property while rural citizens continue to get no support or even no pension at all. If land should also be privatized in the future, proceeds should partially go to the farmers. Initial subsidies can also be used to subsidized middle-aged participants who otherwise could not reach an adequate pension through their own contributions.

5. Institutionalize Monitoring and Evaluation

The effects of a pension reform should be continuously monitored and evaluated. A special board or commission of experts should be set up to produce an annual report. These reports could also help decide which steps to take in the process of stepwise building up a pension scheme (see section A). Reports should not be restricted to public pensions but should include general indicators of social security among the elderly. In particular, if family support and land use are called upon as main pillars of living for the elderly then the active performance of these traditional sources of support should be measured empirically and monitored on a continuous base.

Last but not least, further research on the matter is needed. In contrast to the report on urban pensions, this report on rural pensions rests only on the work of one international expert from one discipline, supported by one domestic expert. A larger research team from several disciplines will be needed. Topics for such research could include the following.

- A survey on the living conditions and the attitudes of farmers with special reference to public and commercial insurance, inquiring, e.g., into the acceptance and the incidence of commercial insurance, into life planning in general, into risk behavior and subjective conceptions of security.
- Dynamic modeling of the changing financial situation of rural pension schemes during the next decades.¹¹
- Institutional details from European legislation, e.g., on the integration and coordination of rural and nonrural systems and on the portability of pension entitlements between different countries.

¹¹ See Lin (1994) for a simulation study of future dependency ratios in the PRC population and related needs for old-age security.

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