

Research on the Incentive Payment Policy of “More Benefits with Longer Payment Period” in China

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Abstract: China established a unified basic old-age insurance system for urban and rural residents in 2014. Although it is a milestone in the social security system for a populous country like China, there are still many problems in the actual operation process, of which the short payment period is the significant problem. The purpose of this paper is to analyze the policy implemented by Chinese local government for urban and rural residents to encourage the extension of payment period policy, to demonstrate whether the policy can effectively let individual participate in the insurance payment earlier, and as long as possible to contribute. At the same time, since bank savings deposits is still a relatively common way of personal capital accumulation for the Chinese people, between contributing more or depositing in the bank, which one will the individuals choose? With government subsidy, will it improve the level of old-age security currently? This paper will illustrate through policy simulation.

1. Introduction

In 2014, China established a unified basic old-age insurance system for urban and rural residents, which merged the new rural social endowment insurance system and the old-age insurance system of urban residents. The system has institutionally covered the rural residents and flexible employment individuals in towns and cities. This is a milestone in the social security system for a populous country like China. Although it has covered total Chinese people, there are still many problems in the actual operation process, of which the short payment period is the significant problem. In prior research, some surveys have shown that in insured individuals, the number of people over the age of 45 is significantly more than under the age of 45, and most of them only reach the minimum payment period of 15 years. This will result in a relatively short payment period. Compared with the mandatory payment of Endowment Insurance System of Urban Workers in China, assuming that an individual retires at the age of 60, the payment period is at least 15 years less. This shows that among urban and rural residents, the contribution payers over the age of 45 have a strong insurance participation consciousness, but those under the age of 40 do not have a strong awareness of it. Considering the international goal of maintaining the adequacy of pension insurance, it is clear that a shorter payment period cannot achieve this goal. In recent years, many

countries have advocated an extension of the retirement age, considering that if the payment period is extended, the total amount of contribution could be increased, and the collection time can be reduced and pension amount will be declined [1] [2].

Since the unified basic pension insurance for urban and rural residents promoted in China is for those who are at least 16 years old (excluding students in school), non-state organs and public institution staff, and urban and rural residents who are not covered by the basic pension insurance system for employees, therefore this system is voluntary and not mandatory. If the Chinese government can encourage these qualified people to join the system earlier through certain incentive policies, this can effectively lengthen the payment period, and increase the accumulation of individual contributions.

Zhejiang Province of China has introduced a relevant policy to encourage the extension of the payment period, which is the contribution period subsidy, so the purpose of this paper is to analyze the policy implemented by Chinese local government for urban and rural residents to encourage the extension of payment period policy, to demonstrate whether the policy can effectively let individual participate in the insurance payment earlier, and as long as possible to contribute. At the same time, since bank savings deposits is still a relatively common way of personal capital accumulation for the Chinese people, between contributing more or depositing in the bank, which one will the individuals choose? With government subsidy, will it improve the level of old-age security currently? This paper will illustrate through policy simulation.

2. Analysis of the Incentive Payment Policy of “More Benefits with Longer Payment Period” in CHINA

2.1 Historical Development and Current Situation of the “More Benefits with Longer Payment Period” Policy

The existing payment incentive policy can be traced back from the new rural old-age insurance policy. In 2009, when the new rural old-age insurance system began to be piloted, it clearly stipulated that the fund consisted of individual contributions, collective subsidies and government subsidies. Under the individual contribution account, it is clearly proposed that the insured will choose the grade of contribution independently, and pay more when getting more. Therefore, although the contribution level set in the national trial plan that year was relatively low, only from RMB ¥100 to RMB ¥500, every 100 for an interval, a total of five contribution grades. However, local governments can increase the contribution level according to the actual situation, and the state can adjust it in a timely manner according to the increase of the net income per capita. This lays a policy foundation for the hierarchical nature of individual contributions. Under the two implementation policies of collective subsidies and government subsidies, the guiding opinions propose that qualified village collectives should give subsidies to the insured persons to pay the fees; local governments should give subsidies to the insured persons, and the subsidy standard is not less than RMB ¥30 per capita per year. For those who choose a higher contribution grade, appropriate encouragement may be given, and the specific standards and methods shall be determined by the provincial (district or county) government. For groups with difficulties in payment such as severely disabled persons in rural areas, local governments should pay part or all of the minimum level of contribution grade on their behalf. Obviously, government subsidies for incentive payment have already played a very important part at that time, but the policy did not mention the incentive for payment period. In the clause of pension treatment conditions, it was proposed to guide young and middle-aged rural residents to actively participate in old-age insurance, to encourage them to contribute in the long term, to implement the policy of “more benefits with longer payment

period”, so government subsidies are applied to incentive payments. However, for the majority of rural residents, the piloted old-age insurance has created a policy precedent in rural areas, and government subsidies have greatly increased the sustainability and robustness of the new rural old-age insurance system, and also clarified the responsibilities of the government in rural pensions.

Subsequently, Zhejiang Province, as an economically developed province on the eastern coast of China, its social security policy has been more innovative, ranking at the forefront of the country. Under the pilot program of the whole country, in 2009, the payment incentive mechanism in Zhejiang Province was specified according to the provincial conditions. The policy of the contribution period subsidy was implemented according to the principle of "More Benefits with Longer Payment Period". Specifically, the policy stipulates that the contribution period subsidy is linked to the length of the insured's contribution period, and is calculated and paid according to the number of payment years, starting from 2010 tentatively set as: the insured person who has contributed for less than 5 years (including 5 years) shall be subsidized RMB¥ 1 per year for the monthly contribution period subsidy; for those who have contributed for more than 6 years and less than 10 years (including 10 years), the monthly contribution period subsidy will be paid by RMB¥ 2 per year from the 6th year; and the monthly contribution period subsidy for more than 11 years (including 11 years) will be paid as RMB ¥ 3 per year from the 11th year. At the beginning of the system, it can be seen that in order to attract more insured people to the system, the Zhejiang Provincial Government spared no effort to target rural residents over the age of 45, as their contribution period is less than 15 years, so subsidies are even given to those less than 5 years of contribution. The subsidies are given for divided 3 time periods from RMB¥1 to RMB¥ 3 subsidies.

In 2014, after the merger of the new rural old-age insurance and the urban old-age insurance, the government of Zhejiang province subsidies continued to be calculated and accumulated according to the contribution period, but the amount of subsidies has been greatly increased, and the specific “More Benefits with Longer Payment Period” policy has been changed as the followings: For those whose contribution period is 15 years, the monthly contribution period subsidy is RMB¥30; If the contribution period is more than 16 years, the monthly contribution period subsidy is added RMB¥5 per month based on RMB¥30, and from the 16th year onwards, the payment period is increased by one year, and an additional RMB¥5 is issued.

2.2 The Theoretical and Practical Significance Analysis of the “More Benefits with Longer Payment Period” Policy

First of all, from a theoretical point of view, the policy of the “More Benefits with Longer Payment Period” links individuals' cross-period consumption and intergenerational transfer payments, which is a process of rebalancing the two distribution methods, and it is the government's use of intergenerational transfer methods to encourage individuals to consume across periods.

From the perspective of improving the goal of adequacy, since the basic old-age insurance system for urban and rural residents implements a system model that combines the social pooling and individual account, hence it is divided into the basic pension accounts and the individual pension account. It is critical to increase individual contributions and the basic pension together. The Chinese government pays basic pensions after the insured reaching the retirement age. According to the regulations, individuals participating in the old-age insurance for urban and rural residents are at least 60 years old and have paid 15 contributions cumulatively, without the basic old-age security benefits stipulated by the state, can receive the old-age insurance benefits on a monthly basis. Since the basic pension is paid after retirement by government finance, it is implemented as a pay-as-you-go system, while the individual account implements an accumulation system. The pay-as-you-go system distributes pensions between generations through financial

transfer and other means, while the individual account system smooths the consumption of personal funds in a cross-period, to accumulate the personal contributions at a young age and to consume in old age [3]. Therefore, if the government can use the incentive contribution policy to link the two systems, it is theoretically a rebalancing process of the two distribution methods. In fact, the government uses intergenerational transfer payments to encourage individuals to make intertemporal consumption [4].

Secondly, in a realistic sense, the policy of the “More Benefits with Longer Payment Period” needs to be attractive enough to let the majority of urban residents and rural residents join the old-age insurance system as soon as possible, at the same time, for the insured who are already in the system, it is significant to let them insist on continuous payment.

From the perspective of attraction, if the benefits brought by the contribution of social insurance can be greater than the bank savings, it would be a very big attraction, because the pension security is also obtained compared to single bank savings.

3. Comparison of the Differences between the Effect of the “More Benefits with Longer Payment Period” Incentive Contribution Policy and Bank Savings Deposits—— based on Policy Simulation

For the Chinese people, the bank saving is still a relatively common form of personal capital accumulation, especially for lower-income and middle-income people. Therefore, in the case of government contribution subsidies, if to compare insurance contributions with bank savings, which is a traditional way of accumulating wealth for the elderly, will individuals choose to increase the number of contribution years or bank savings deposit? Currently, which way will improve the level of pension security? Here’s a comparison through policy simulation.

First, because of the policy changes in Zhejiang Province, the policy in 2014 is mainly used here for simulation. That is, in order to encourage the extension of paying contributions, the government subsidies RMB¥ 30 yuan for 15 years, and gives RMB¥5 more per month for every additional contribution year on basis of 15 years. In order to evaluate the effect of the incentive policy, it is necessary to compare the total yield of the extended contribution with the yield of bank savings deposits. Hence, the hypothesis is that if the former has higher returns than the latter, incentives will work.

The specific assumptions are as follows:

(1) Assuming there are 16 contribution years

For the sake of comparison, it is supposed that an individual pays the contribution for 16 years before the age of 60.

In order to have more time to contribute before the age of 60, if the insured person wants to pay an extra year’s premium on the basis of 15 years, it is assumed that the contribution is paid at the age of 44, so, at the age of 58, the contributory years are 15 years. Then, the 59th year old can choose to continue to pay an extra year of premiums, which can be paid when he reaches the age of 60 after one year.

(2) Assumptions for the interest rate of bank deposits

In order to take into account the yields of contributions, two parts of the yields need to be considered, one is from the contribution period, the other part is from the pension issued by the government as the contribution period subsidies in the basic pension account.

According to the provisions of the Social Insurance Law of the People’s Republic of China, the interest rate of the bookkeeping shall not be lower than the interest rate of the bank’s fixed deposits, and the interest tax shall be exempted. Based on the ten-year fixed deposit rate, it is assumed that the bank deposit rates with 1.50%, 2.0% and 2.5% three grades.

(3) Assumptions for the contribution period subsidy

The subsidy issued by the government is divided into two parts, one part is the subsidy of RMB¥30 monthly for reaching 15 years of contribution, it is RMB¥ 360 in one year; the other part is the subsidy for the contribution period which is more than 16 years, based on RMB¥ 30, RMB¥5 per month for each additional contribution year on basis of 15 years. Therefore, assuming that an insured resident pays the contribution before the age of 60 for 16 years, the individual can receive a monthly pension subsidy of RMB ¥35 yuan after retirement.

(4) Assumptions for monthly divisor

According to the provisions of the Chinese Social Insurance Law, the monthly divisor is 139, so it is assumed that the number of payment months is 139 after the age of 60, which equals to 11.58 years. Although the life expectancy of Chinese has far exceeded 71.58 years old, it is followed by the state finance after the number of months, therefore it is no longer measured.

(5) Assumption for contribution grade

According to the national contribution grade plan, it is assumed that there five contribution grades, including RMB¥100, 200, 300, 400, 500 respectively.

Based on the above assumptions, this article uses the first year's contribution to be bank savings, which need deposited for 27.56 years (16 years plus 139 months) with the payment of the first year, then to compare this with the sum of the contribution period subsidies which could be received at least 139 months. The specific simulation results are shown in the following tables.

As can be seen from table 1 and table 2, the amounts of regular bank savings interests accumulated by different interest rates are all far lower than the subsidy of RMB¥4380 for 15 years of contribution, even is lower than the accumulation RMB¥695 of RMB¥ 5 per month, and is much less than the total accumulation of RMB¥5075 of pension subsidies totally.

It should be noticed that as the distribution standard of the contribution period subsidy is the number of the total contribution year, it is not related with the contribution grades, so the subsidies in table 2 are the same among different contribution grades.

Table 1 Interests on bank savings deposits by contribution grade

Unit: RMB YUAN

Contribution grade	Bank Interest Rates		
	1.50%	2.00%	2.50%
100	50.78	72.67	97.61
200	101.56	145.34	195.22
300	152.35	218.01	292.82
400	203.13	290.69	390.43
500	253.91	363.36	488.04

Table 2 Sum of contribution period subsidies calculated by contribution grades

(16 contribution years)

Unit: RMB YUAN

Contribution grade	15 contribution years	1 more contribution year	Contribution period subsidy
	Subsidy	Subsidy	Subsidy
100	4380	695	5075
200	4380	695	5075
300	4380	695	5075
400	4380	695	5075

500	4380	695	5075
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As shown in table 3, there are also the rates of return calculated by the contribution grades. What does it mean? This means if one individual wants to get the same interests by bank savings deposits as the contribution subsidies, then the rate of interest should get to the simulated levels in table 3. It is apparent that with the increasement of the contribution grades, the calculated yields are reduced, but even the lowest yield of subsidies for one more year of extended contribution also reaches 3.21%, if adding the government subsidies for 15 years of contribution, the total minimum yield of the pension subsidies can reach 9.14%, which is much higher than the bank interest rate of 1.5% at this stage. In China's history, there have been few years when such a high interest rate on bank deposits has been reached.

Table 3 The yield of contribution period subsidy calculated by contribution grades
(16 contribution years)

Unit: RMB YUAN

Contribution grade	15 contribution years	1 more contribution year	Contribution period subsidy
	Rate of return	Rate of return	Rate of return
100	14.78%	7.81%	15.38%
200	12.02%	5.58%	12.60%
300	10.47%	4.44%	11.03%
400	9.41%	3.72%	9.95%
500	8.61%	3.21%	9.14%

4. Conclusion

In conclusion, it is significantly indicated that government subsidies for extending contribution years can improve dramatically the pension security levels, especially for the lower-income groups, because the subsidies for extending contribution years have higher yields than the traditional bank saving deposits, and for the insured who choose the lower contribution grades, they could have more benefits than the other higher contribution grades, as the amounts of subsidies discussed in this article is determined by contribution years not contribution grades. Therefore, it is suggested that the lower-income insured should insist on contributing, if the governments in China could help contribution for them in the long term, this will alleviate the aging pressures. At the same time, for the other higher income groups, it is necessary for them to contribute earlier to get more support from government as well. Of course, maybe some urban and rural residents do not know the higher benefits of earlier contribution, it is necessary for the governments to advertise this and have more communications with them to let they understand the polies deeply and improve their financial consciousness.

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