Towards Greater Coverage and Sustainability of the Social Security System in the Philippines¹

Abstract

At the request of the Philippines Social Security System (SSS), the World Bank prepared a report to analyze key challenges and propose reform options to improve the sustainability and expand the coverage of old age income protection for private sector workers. Projections employing the Pension Reform Options Simulation Toolkit (PROST) found that the SSS scheme will face outflows greater than inflows in about 20 years and depletion of its assets in about 28 years. Fortunately, its medium-term financing issues can be addressed through the gradual introduction of parametric reforms that shield workers and retirees from abrupt changes in contributions and benefits. At the same time, the Philippines faces a challenge to improve the de facto coverage of workers by Social Security, and to increase the income protection coverage of the elderly. Options suggested include SSS measures to leverage its identification system and introduce a special instrument for informal workers. Rather than introducing matching contribution subsidies to expand coverage, it was suggested to broaden the scope of beneficiaries eligible for social pensions. Beyond the scope of the SSS, additional measures were suggested including those to improve the access and efficiency of contributions and payments systems, strengthening mobile-money platforms and efforts to improve access to savings instruments, particularly for small and isolated savers. The note points out that the key means of improving coverage lies beyond the scope of social security or pensions, namely, to improve the quantity and quality of wage-based employment.

I. Introduction

This note summarizes a report prepared in 2015-2016 for Philippines Social Security System (SSS) that administers mandatory social security for the private sector workers in the Philippines. It addresses two concerns: (i) how to increase the de facto coverage of social, and (ii) how to ensure long term sustainability of the SSS.

II. Demographic and Economic Conditions

A. Demographic Profile

The projected demographic trends signal that the Philippines will be facing the challenge of an aging population in the not so distant future. The old-age dependency ratio (those over age 60 as

¹ This note was prepared by Mark Dorfman and Tatyana Bogomolova of the Social Protection and Labor Global Practice of the World Bank. The note is based on the report: Republic of the Philippines: Review of the Social Security System, Considerations for Strengthening Sustainability and Coverage, World Bank, 2016.
a proportion of those who are working-age) is projected to almost double from about 12 percent in 2015 to 22.5 percent in 2050 (Figure 1). The aging of the population is projected to impact the economic and social landscape and the way people work and live, including on labor market participation, the social security arrangements and their sustainability, the cost of health and elderly care and so on. The good news is that the Philippines is still a young country, with opportunities to respond to the gradual aging.

**Figure 1: Population by Broad Age Groups**  
(Millions – left axis, and percent right axis)

![Population by Broad Age Groups](image)


Workers covered by the SSS have considerably higher old age dependency ratios when compared with the broader population, which is a key determinant in the sustainability of the SSS scheme (Figure 2). This is consistent with trends in other countries in the region, as fertility rates among the covered population tend to be lower than for the population as a whole, and life expectancy at retirement age also tends to be higher. This may be that the current contributors and beneficiaries tend to be wealthier urban workers who have lower fertility rates and higher life expectancies and belong to the group of workers with formal employment and stable tenure.

**Figure 2: Projected Population and SSS System Dependency Ratios**  
(Percent)

![Projected Population and SSS System Dependency Ratios](image)

*Source: World Bank estimates, UN World Population Prospects, the 2012 revision.*

In about quarter of a century, increases in the SSS old age dependency ratio along with flattening of the relative size of the working-age population will begin to have significant implications for pensions and social security policy. SSS will face increasing outflows due to increasing numbers of retirees. At the same time, they will face moderating inflows as the number of contributors will be limited by the delayed effects of declining fertility rates. At the household level, families will have to support more retired members with a smaller ratio of working household members to those too old to work.
B. Labor Markets and Social Security

The Philippine labor market is characterized by high levels of informality. The World Bank has estimated that around 75 percent of Filipino workers are informally employed. The National Statistics Office (NSO) and the Department of Trade and Industry (DTI) estimate that around 90 percent of Filipinos work in micro, small, and medium-size enterprises (MSME) or as own-account workers. Operationally, the informal sector includes the agriculture and informal services sectors, the latter of which includes wholesale and retail trade, transportation, communication, and storage.

Although wage and salaried workers account for about 55 percent of total employment, many of these workers do not contribute to the SSS, and many do not receive adequate protection under the Labor Code. Only about 38 percent of wage workers indicate that they contribute to the SSS or GSIS. Agricultural workers have the highest degree of informality, with more than 90 percent of workers experiencing low levels of protection and high levels of income insecurity.

Such high levels of informality can be explained by both worker characteristics and the nature and composition of jobs. Barriers to employment generation include a weak investment climate and costly business, tax, and labor market regulations. Workers also have a limited skill set, in part due to the substantial outmigration of skilled workers. The result is that “the vast majority of workers have remained trapped in low-wage and low-productivity jobs in the informal sector, with limited opportunities to move up the job ladder.”

The high level of informality and wage distribution have important implications for social security participation. There are significant and understandable challenges in the enforcement of contribution compliance requirements in an environment characterized by high levels of informality. Weak enforcement leads many employers either not to participate or to selectively participate only for long-term workers. This is aligned with workers’ interests to the extent that employees may also seek to avoid remitting employee contributions or may collaborate with employers to under-report wages. Moreover, very limited job security, low wages and other potential risks such as loss of health generally leads workers to prefer immediate compensation rather than waiting until retirement. Short-term risks such as loss of income or health, or investment in children’s education may tend to be much higher priorities for workers than saving for retirement.

C. Elderly Living Arrangements and Sources of Income

Living arrangements and sources of income are important to elderly vulnerability and poverty and thus have implications for the design of contributory pensions or non-contributory social assistance. Elderly living with non-elderly potentially have access to the labor income of non-elderly, but they are similarly vulnerable if there is insufficient income or if the household falls into poverty. Such undiversifiable risk is one of the rationales for elderly assistance programs such as the Social Pension scheme in the Philippines.

In terms of income sources, labor force participation is noticeably high among the working-age population, particularly at higher ages, indicating the importance of labor income to households. Total labor force participation peaks during the ages of 45-54, although men are beginning to leave the labor force as women continue to increase their participation (Figure 3). By ages 55-64, total labor force participation remains at almost 70 percent. Although elderly Filipinos are employed less as they age, labor force participation remains high until they are unable to work. About one-third of workers ages 75-79 report to have worked.

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2 See World Bank, Philippine Development Report: Creating More and Better Jobs, September 2013, p. 72 and World Bank, Republic of the Philippines, Labor Market Review, Employment and Poverty, Report Number: AUS8661, January 22, 2016.. The report defines informal workers as including self-employed workers (not including employers); unpaid family workers; and wage workers with no written contract, social insurance, or protection from dismissal. The data source was the 2008 Informal Sector Survey (ISS) 62 of the National Statistics Office (NSO). Administrative data on the population covered by SSS by firm size was not available.


4 In work poverty is pervasive in the Philippines. See World Bank, ibid.

5 This section was substantially limited by the absence of household survey data that indicates the sources of individual income tabulated by five-year cohorts.
As Filipinos age, they increasingly move into self-employment and employment in family operations. As Filipinos reach the legal retirement age of 65, their relative employment in government and private enterprises declines substantially from about one-third to about 21 percent at ages 75-79, with further decline for older workers. Among older workers with employment income, self-employment income grows from about 58 percent of the total for those ages 58-64 to over 75 percent for those age 80 and above. The proportion of elderly that are employed understandably falls from 65 percent from ages 58-64 to only 15 percent at ages 80 and above as individuals lose the capacity to work.

D. Poverty and Inequality

Poverty incidence in the working-age population provides some indication of the difficulty individuals have in contributing to payroll-tax based social security arrangements. As of mid-2014, about one-fifth of households and about one-quarter of individuals in the Philippines fell under the national poverty line. Rural and agricultural workers are particularly vulnerable to poverty and represent the bulk of the working poor as well as urban workers who have informal and low-skilled jobs who are vulnerable to poverty. Labor force status has little impact on the risk of poverty and indeed the majority of working age poor are employed. Workers in private households (such as domestic workers) and family-operated businesses or farms—who comprise relatively smaller proportions of the total population—have the highest poverty incidence. Understandably, the self-employed have higher risk of poverty when compared with wage workers in both rural and urban areas.

Poverty incidence among the elderly was lower than for other age groups, possibly because of family support/living arrangements and accumulated assets. In 2013, poverty incidence among the elderly (11 percent) was significantly lower than the national average (over 25 percent), lower than for the working-age population and was less than half that of children age 14 and under (29 percent) (Figure 4). This pattern, which is consistent with many countries worldwide, may be partly explained by many elderly having children to support them and some having accumulated assets in retirement. As of 2013, almost half of the poor in the Philippines were children, while only 5.7 percent of the total were elderly. From a policy perspective, this distribution of poverty suggests that scarce resources for transfers should consider poverty prevalence across lifecycle when using the age of recipients as an eligibility criteria.

Figure 4: Poverty Headcount Incidence and Share by Five-Year Cohorts (Percent)

In addition to the challenge of poverty, the Philippines faces high levels of income and welfare inequality. The income Gini coefficient for the Philippines was 48.0 in 2012, one of the highest in the region. Almost half of the income was received by those in the top quintile, while those in the bottom quintile received about 6 percent.

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9 Ibid, p. 50-51.
10 This calculation used the national poverty line, which represents the bottom 20 percent of the income distribution for the entire population.
III. Social Security and Pension Programs for Private Sector Workers

A. Social Security System

1. Description

The SSS is a defined-benefit scheme for private sector employees, including the self-employed. The scheme has three benefit formulas, essentially providing the best of: (i) 40 percent of the wage base for those with 10 years of contributions, (ii) PHP 300/month + 20 percent of the wage base for 10 years and 2.0 percent per year of contributory service for each year thereafter, or (iii) PHP 1,200/month. Annuity benefits can be received after 10 years of contributions at age 60 for most workers, 55 for miners, and 65 for the self-employed. Age 65 is the mandatory retirement age. Indexation is discretionary based on the observed level of inflation and the financial position of the fund. The minimum pension depends on the years of contribution, with a minimum benefit of PHP 1,200/month after 10 years of contributory service and PHP 2,400/month after 20 years of contributory service.

The SSS is a partially funded scheme with mandatory contributions. Contribution rates are 7.4 percent for employers and 3.6 percent for employees, or 11.0 percent total for both. The self-employed pay the full 11.0 percent contribution. Although there is a minimum covered wage of PHP 1,000/month, this is waived for participants in the AlkanSSSy program for informal sector workers, described below. The maximum covered wage is PHP 16,000/month or about 100 percent of the average wage for covered workers.

2. Coverage

Although de-jure worker participation in the pension schemes is mandatory, actual or de-facto coverage rates are low. The legal requirement for participation extends to all workers including self-employed, temporary, and informal sector workers. Only about 25 percent of the employed contribute on an active basis to the SSS. In 2013, about 17.8 percent of the working-age population and 25.8 percent of the labor force had contributed more than a month to either the SSS or GSIS. With this low labor force coverage, elderly coverage has also been challenging, albeit the Philippines has been fortunate to have a non-contributory Social Pension which protects the poorest elderly from poverty.

The average density of SSS contributions in the Philippines is relatively low, suggesting that many workers are not participating for a substantial portion of their work lives. The average contribution density at retirement was about 26.5 years in 2013.

The SSS has made substantial efforts to increase coverage by expanding the scope of employers and workers required to contribute. The self-employed were required to contribute beginning in 1980, with self-employed professions then expanding to farmers, fisherman, and others in the 1990s. However, the actual implementation of the legal mandate for coverage has been costly and difficult to enforce, largely due to prevailing informality and non-contract, intermittent employment.

The SSS initiated measures several years ago to make it easier for informal sector workers, the self-employed, and voluntary contributors to contribute. The SSS also began to accredit cooperatives as collection agents for self-employed and voluntary contributors in 2011.

In 2012, the SSS launched the AlkanSSSy program with the aim of broadening the actual coverage to include the self-employed and informal sector. The program targets low- and limited-income workers such as tricycle drivers, farmers, market vendors, fishermen, and other self-employed individuals. It aims to establish a piggy bank-like savings program in which the daily discipline of contributing at least PHP 10 could, over time, support a meaningful level of social security benefits. After three months of contributions, members are entitled to sickness, maternity, or funeral benefits. Educational loans are available after 12 months of contributions, disability loans after 36 months, and a pension claim after 10 years at retirement age.

11 World Economic Indicators, accessed October 2015.
12 The minimum covered wage ranges from about 200 to 400 percent of the legal minimum wage, which varies by region. See Department of Labor and Employment, National Wages and Productivity Commission, 2016, http://www.nwpc.dole.gov.ph/pages/statistics/latest_wo.html
13 See Meißner, Matthias, Old age protection for informal workers–feasible or too far away? March, 2014.
The SSS has partnered with informal sector groups (ISGs) and worker associations to facilitate collections and to market the AlkanSSSy program. Associations such as the association of tricycle drivers have helped serve as channels for worker registration, collections, and information disclosure. The SSS has also established a system of savings bank boxes at various locations where workers can deposit their daily contributions. At the end of 2014, the SSS had an estimated more than 122,000 members participating through over 1,200 ISGs.\textsuperscript{14}

3. Sustainability

Baseline PROST projections of SSS system finances suggest that the SSS faces a challenge to achieve long-term sustainability, albeit some time to adopt parametric reforms to address the challenge. Financial surpluses are projected for roughly the next 20 years, after which time projected deficits would eliminate fund assets about eight years later (Figure 5).\textsuperscript{15} The projected fund life for the SSS is therefore about 28 years extending to about 2044.\textsuperscript{16} Projected system finances deteriorate over time, as the SSS system old age dependency ratios increase, leading to payouts in excess of revenues of over 1.0 percent of GDP by about 2060.

\textbf{Figure 5: SSS – Baseline Projection of Pension System Finances} \\
\textbf{(% of GDP)}

\begin{center}
\includegraphics[width=\textwidth]{figure5.png}
\end{center}

\textsuperset{Source: World Bank estimates.}

Much of the projected deterioration in the sustainability of the SSS stems from an aging profile of contributors and retirees along with a benefit formula and qualifying conditions that over time cannot be fully supported by contribution levels. An important driver is the projected number of contributors and retirees (Figure 6). The SSS is a maturing scheme, with many of its initial participants having reached or reaching retirement. The relative growth of the retiree and beneficiary populations will become more rapid during the projection period, resulting in growing system dependency ratios. These increasing system dependency ratios result in projected benefit payments that over time are higher than contributions and investment returns.


\textsuperscript{15} These projected estimates are based on several assumptions such as anticipated coverage levels, growth in real wages, and real returns on investment assets. Actual outcomes will likely differ from the projections to the degree that the underlying assumptions differ from actual experience.

\textsuperscript{16} The fund current balance is defined as: (contributions + investment income) – (benefits paid + other expenses). The fund life is defined as the number of continuous years during which projected fund assets are positive.
4. Risk Coverage and Equity

Discretionary indexation of SSS benefits has failed to keep up with inflation over the past two decades, affecting adequacy. Indexation on average covered only about 60 percent of growth in the consumer price index (CPI) over the past two decades. Moreover, there were substantial multi-year lags between the adoption of indexation adjustments.

In terms of equity, the distribution of pension income is concentrated in higher-income households (Figure 7). Almost half of the share of contributory pension benefits goes to those in the top decile of the income distribution, and almost 80 percent of the share goes to those in the top three deciles. Not only is the share of pensions concentrated in the upper deciles, but pension income as a proportion of household income also is highest in the upper deciles, with pension income representing almost 5 percent of total income for the top decile.

Figure 7: Benefits from Contributory Pensions
Proportion of total household income & share of total

Source: NSO, Family Income and Expenditure Survey 2011, Table 3, Number of Families and Family Receipts by Income Decile.
Note: The data includes all pension payments including those from SSS and GSIS.
5. Identification and Delivery Systems

One noteworthy administrative feature of the SSS (and GSIS) is the use of an identification system for their members, including biometric identification and smart-cards. In 2008, the social security identification system was identified as the core of the Unique Multi-Purpose Identification (UMID) system, and the SSS was instructed to lead in the streamlining and harmonization of the ID systems of all government agencies and GOCCs. Although the UMID card has been characterized as a unified card for transactions of four government agencies, namely: SSS, GSIS, PhilHealth, and Pag-IBIG (Home Development Mutual Fund), the databases are not linked between the agencies and there is no process for deduplication across agencies. In April 2015, the SSS announced the release schedule for its own UMID card, which can be used to view an individual's SSS profile and account, statistical information, SSS premiums, history, SSS loans, and balances.

Importantly, the SSS database has de-duplication/reconciliation processes so that those members with SSS UMID cards can be ensured to be unique. Authentication is done initially through verification of birth certificates and establishment of biometric identifiers. Validation can be done at SSS offices as well as in banks. Inquiries are web-based, with authentication through pin numbers. The database of members will be materially strengthened as the SSS gradually issues UMID cards to replace earlier identification.

Measures have also been taken to improve SSS delivery systems. Registration has been automated online, and contributions and loan repayments can also be done online through two banks, including through a large network of ATMs. An online service portal (My.SSS) allows SSS members to have exclusive access to their contributions and membership records, make online transactions, and request copies of their records as needed. The online portal is not yet available on mobile phones, although efforts are being made to provide it in the near future.

B. Social Pensions

The Department of Social Welfare and Development (DSWD) has provided a Social Pension benefit for indigent senior citizens since 2011. As of 2015, the scheme covered about 940,000 individuals or about 20 percent of those aged 65 and above. Since its inception, the benefit has been PHP 500 (about US$10.70) per month, paid quarterly. The cost in 2015 was about PHP 6.0 billion or 0.08 percent of GDP, having risen substantially since 2014 with a reduction in the age of qualification from 77 to 65.

Aside from being identified as poor by the national household targeting system Listahanan, beneficiaries must meet other eligibility criteria. The beneficiary must be 65 years old and above. Applicants must obtain a Senior Citizen’s Identification Card (OSCA ID) issued by local government units (LGUs). Obtaining such an ID requires other valid identification or a birth certificate.

The benefit level appears to be adequate for many elderly poor. The benefit represented about 8.3 percent of GDP per capita in 2014. Adequacy would depend upon the cost of living and the per capita poverty income gap in each region. While the benefit covers only about 28 percent of the national per capita poverty threshold, it is very close to the poverty income gap on a per capita basis. However, the benefit level is not indexed, subjecting beneficiaries to price risk. No adjustments have been made since it was introduced in 2011 resulting in a decline in the real value of the benefit by about 15 percent.

IV. Parametric Reforms to the Social Security System

The projected medium-term financing issues can be addressed through the gradual introduction of parametric reforms that shield workers and retirees from abrupt changes in contributions and benefits. Each of these reforms have been simulated using PROST. These reforms could include the following (Table 1 summarizes the projection results for each):

- Unify the SSS old-age benefit formula for all vested members to improve the incentives for participation and promote equity among workers with different incomes and lengths of service;

17 The authors are not aware of an applet for web-based communication with SSS for members.

18 Listahanan is a national household targeting system hosted by DSWD. Originally, it was established in 2008 to support the conditional cash transfer program. In 2009/10, data from about 11 million or 60% of Filipino households was collected of which 5.3 million were identified as poor. In 2010, a presidential decree was issued obliging all government agencies to use Listahanan to identify poor beneficiaries of Government’s poverty reduction programs. In 2015, DSWD collected information from 75% of Filipino households (15.1 million) to update Listahanan. Listahanan uses a proxy means testing method to estimate per capita income of surveyed households and provincial poverty lines to identify the poor. The list of poor households are verified by communities for accuracy and transparency, before being finally determined.

19 PROST has been used to simulate these parametric reforms. These simulations provide the basis for an evidence based assessment.
• Replace the discretionary indexation of benefits with full and automatic inflation-based indexation to help protect retirees against inflation during retirement;
• Extend the wage base for determining benefits and “valorize” the wage base according to the average covered wage growth;
• Gradually increase the retirement age to 65 years and increase it in the future in accordance with increases in life expectancy at retirement age;
• Gradually reduce the benefits accrued each year for service after a reform date to a level that achieves sustainability over the long term consistent with the other parameters; and
• The contribution rate could be gradually raised in the future to improve the long-term balance, although any increases need to be considered in the context of the overall tax wedge.

Table 1: Summary of the Financial Effects of SSS Baseline and Simulated Reforms

<table>
<thead>
<tr>
<th>Reform scenario</th>
<th>Financing gap*</th>
<th>Break-even point**</th>
<th>Assets depletion point***</th>
</tr>
</thead>
<tbody>
<tr>
<td>baseline (no reform)</td>
<td>(34%)</td>
<td>2036</td>
<td>2044</td>
</tr>
<tr>
<td>Package 1</td>
<td>(48%)</td>
<td>2030</td>
<td>2038</td>
</tr>
<tr>
<td>Package 2</td>
<td>(36%)</td>
<td>2037</td>
<td>2046</td>
</tr>
<tr>
<td>Package 3</td>
<td>(23%)</td>
<td>2040</td>
<td>2049</td>
</tr>
<tr>
<td>Package 4</td>
<td>(11%)</td>
<td>2054</td>
<td>2063</td>
</tr>
<tr>
<td>Package 4a</td>
<td>(1%)</td>
<td>2068</td>
<td>2079</td>
</tr>
</tbody>
</table>

*Present value of cash flows over a 75 year period expressed as a percent of 2013 GDP, with 4% real discount rate.
** Year when the annual current balance turns negative.
*** Year when Pension Fund’s own assets are depleted and government needs to step in to cover deficits.

Reform packages (reform starts in 2017):
• Package 1: (i) harmonizing benefit formula for all (moving to PHP 300 + 2% per year of contributions for any number of years of contributions = 10 and above; introduced gradually over 5 years); (ii) moving from 5-year average wage (not valorized) to lifetime average wage valorized to wages as the income measure used in pension calculations; and (iii) introducing full inflation indexation for post-reform pensions (instead of current average trend of annual average at about 60% of inflation rate).
• Package 2: Package 1 + increase retirement age (to age 65 over 10 years, then gradually to age 68 by 2080)
• Package 3: Package 2 + accrual rate reduced to 1.5%, applied to post-reform years of contribution
• Package 4: Package 3 + contribution rate increased to 15% between 2031 and 2035 (by 1 p.p. per year
• Package 4a: Package 3 + contribution rate increased to 18% between 2031 and 2035 (by 1 p.p. per year)


The parametric changes simulated are proposed as a starting point to further evaluate a combination of reforms that best weighs the tradeoffs between fiscal cost, sustainability, adequacy and coverage suggested. Projections can be useful in helping policymakers identify the package of parametric reforms that would best meet their objectives for the SSS.

Reform Package 1 aims to improve the incentives for participation and to promote greater equity among workers of different incomes and different service lengths. This would include: (i) harmonizing the accrual rate and equalizing the incentives for workers to contribute regardless of their service histories; (ii) extending the wage base and valorizing the base according to covered wage growth; and (iii) establishment of an automatic inflation indexation of benefits to protect retirees from inflation during retirement. Together, these three parametric reforms would worsen the financing gap by about 14 percentage points and move up the break-even point from the baseline 2036 to 2030 (Table 1, Figure 8).

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20 This would be a gradual process whereby the salary reference period could be increased at a pace consistent with recordkeeping capacity, such as increasing the wage base at a pace of one year per year after the reform is established.
The second reform would gradually increase the minimum retirement age from 60 to 65 and therefore increase incentives to work longer and improve sustainability (Table 1, Figure 8). Subsequently, the retirement age could be increased to in line with increases in life expectancy at retirement age to maintain a life expectancy of 15 years at retirement. Increasing the minimum retirement age by 5 years would decrease the projected years in retirement by about 3.4 years thereby improve SSS financial sustainability. Increasing the retirement age results from the gradual decline in the fertility rate among the SSS-covered population and the increase in life expectancy. The benefit provided for retirees retiring earlier than the minimum retirement age should be subject to an actuarially fair benefit penalty, and those retiring after the minimum retirement age should receive an actuarially fair supplement that would have the effect of ensuring actuarial fairness of benefits among those retiring at different ages, therefore removing the current disincentive to work longer. The penalties and supplements would also enable workers to make retirement choices that fit their needs and circumstances.

![Figure 8: SSS – Impact of Reform Packages on Sustainability – Annual Current Balance (Percent of GDP)](image)


![Figure 9: SSS – Impact of Reform Packages on All Retirees’ Replacement Rate (Percent of average full wage for all retirees)](image)


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21 Although we chose a target life expectancy at retirement of 15 years, other targets could also be modeled and considered. The logic of aligning the retirement age with life expectancy at retirement contributes to a financial balance by maintaining a fixed number of years in retirement as life expectancy increases at the retirement age.

22 These figures are based on mortality for the entire country. Cross-country data suggests that it is very likely that the SSS retirees have longer life expectancies at retirement ages.

23 In addition, the labor law provides for mandatory retirement at age 65, which this analysis suggests should be eliminated.
The third reform package, which would gradually reduce the marginal accrual rate, would result in a gradual reduction in replacement rates at retirement and some strengthening in system finances (Figure 8, Figure 9). The replacement rate and financial flows would be only fully adjusted after about 40 years. The impact on the financing gap would be a reduction (from the scenario for Package 2) from 36 percent of GDP to 23 percent.

The fourth reform package illustrates the quantitative effect of an increase in the total contribution rate from 11 percent to 15 percent (Figure 8, Figure 9). Such an increase begins in 2031 under the assumption that it would make limited sense to levy a contribution increase in the short term based on financial flows that only become negative over the long term. This package of contribution increases need to be considered in the context of the overall tax wedge as discussed further below.

Finally, a variant on the fourth reform package was modeled which increases the total contribution rate sufficiently to eliminate the projected financing gap by 2080 (Figure 8). Eliminating the financing gap would require an 18 percent contribution rate beginning in 2031.

Although periodic increases in the contribution rate were enacted in the past to improve sustain-ability, future increases should be considered in the context of the overall tax wedge, as such measures will likely affect worker coverage and compliance. The tax wedge is the overall set of additional costs of labor in addition to wages and includes social security contributions, health insurance contributions, personal income tax rates, severance payments, the cost of minimum wage policies, and any other non-wage labor costs. Marginal tax rates are steep, so just these costs represent a substantial cost for labor and create a strong incentive for wage under-reporting and tax avoidance. It is therefore important to model different levels and timing of increases in the contribution rate and reductions in the marginal accrual rate to see which mix can best achieve the sustainability objective, while also managing the affordability of contributions and adequacy of benefits.

V. Options to Consider to Improve Coverage

A. Overall Considerations to Increase Social Security Coverage and Income Protection in Old Age

Measures to increase worker coverage are needed to increase the probability that workers will have a steady source of income from social security once they reach old age. Support elderly receive from other household/family members are subject to non-diversifiable unemployment, health, and natural disaster risks, which the elderly can only diversify with alternative sources of income in retirement. Moreover, the number of elderly is increasing and they are living longer, so household incomes will have to support a growing number of elderly dependents. Finally, workers may be more inclined to take occupational risks and make more risky entrepreneurial investments if they can be assured that they will have some level of income in old age and will be protected from poverty.

Contributory schemes such as the SSS face particular challenges in covering workers that have low and intermittent incomes. Informal workers with low and intermittent incomes face severe constraints in setting aside savings or social security contributions. They also often have needs (e.g., education of children, investment in self-employment or building a house), as well as face risks that may have greater relative importance for savings than smoothing income in retirement. In addition, the delivery system and collections channels may be inaccessible or inefficient, posing important transactions costs.

Given the high degree of informality in the Philippines, aligning social insurance design and delivery system with the needs of informal workers will be critical to expanding coverage. The schematic diagram in Figure 10 below illustrates how generic elements of social insurance design and implementation can be aligned with the needs of informal workers. The diagram shows how savings and social insurance policies and programs can build upon common foundations of identification and delivery systems. Moreover, it points out how micro-savings, social insurance, and health insurance programs can have important synergies in providing risk protection for informal sector workers.

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24 The reduction in the accrual rate by 0.5 percent per year and the timing over five years is meant as a reference point only. The actual reduction and phasing should be calibrated to the circumstances, including the political economy dimensions.

25 As noted above, the level of contribution increase and the phasing are meant as illustrations of the effects. The actual reform parameters adopted should be determined with the support of additional modeling.
The most important and sustainable remedy to improve social security coverage is to improve the quantity and quality of wage-based employment – measures which are beyond the scope of the SSS scheme design or delivery systems. Low worker coverage and contribution densities mirror the limited steady wage-based jobs for most Filipino workers. Low and intermittent incomes often from small companies or agriculture, self-employed or single proprietors present formidable challenges both to economic stability as well as provide a weak basis for contributing to social security. Measures are needed to reduce the barriers to employment generation, which include a weak investment climate and costly business, tax, and labor market regulations. Moreover, weaknesses in skills need to be addressed. Overall, higher productivity jobs are essential for coverage expansion.

**Figure 10:** Stylized Diagram of Building Blocks for Savings and Social Insurance Aligned with the Needs of Informal Workers

B. SSS Measures to Increase Coverage

**Measures to improve SSS program administration could make it easier and more efficient for informal workers to contribute toward social security.** The SSS has already taken steps in this direction, for example with the adoption of Automatic Debt Arrangements to facilitate informal worker contributions and working through intermediaries to extend outreach and manage some of the record-keeping in the AlkanSSSyYa program. Further measures can be taken to substantially increase access through mobile-money based contributions and payments and mobile phone based member interface.

**The identification and management information systems at the SSS can be important building blocks to the inter-institutional delivery platform.** Although a more thorough assessment is needed, in principle, it would be possible to build upon the de-duplication capability of the SSS unified multi-purpose identification card (UMID). The de-duplication capability could, in principle, be leveraged to create a more unified identity across institutions as a foundational identification.

The defined-benefit design of the current SSS scheme may not provide sufficient simplicity and flexibility for informal sector workers. A special instrument for informal workers could be designed to align with their needs and preferences. Such an instrument could be structured as a defined-contribution savings vehicle that also offers annuitized benefits at retirement. Such benefits could be additive to benefits received from the defined-benefit SSS pensions. Pension calculators could communicate projected benefit levels at different retirement ages, including benefits for workers with contributions in both the defined-contribution and defined-benefit SSS schemes. Moreover, partial withdrawals could be permitted in the case of defined events such as extended unemployment, catastrophic health events or disability and natural disasters. Finally contributions should be voluntary and at the level and timing appropriate to each worker (such as the approach with the AlkanSSSyYa program. Together, these features could make such an SSS instrument more attractive than the current defined-benefit SSS instrument for informal workers.
Although several countries have considered matching contribution subsidies to expand coverage, our analysis suggests that this would not be the most effective instrument for coverage expansion in the Philippines as follows: (i) those poor and vulnerable workers who could access the subsidy are unlikely to be able to afford the contribution; and (ii) the fiscal costs could be substantial depending on the benefit level, match and targeting. A more effective alternative would be to use fiscal resources to broaden the scope of beneficiaries who are eligible for social pensions. Over the long-term, with income growth, it may be constructive to revisit the cost-effectiveness of such matching contributions.

C. Beyond SSS – Inter-Institutional Delivery System, Savings Options, and Broadening Eligibility for Social Pensions

Many of the processes outlined in the building blocks in Figure 10 above are common across institutions. In this way, a de-duplicated foundational identification has applications that extend well beyond Social Security and can be equally effective in strengthening Government transfer programs, PhilHealth and can assist in broadening public access to financial intermediation such as through bank or mobile-money accounts. Similarly, an efficient and effective payment system can reduce the cost of the extensive money transfers in the Philippines as well as facilitate contributions from and payments to the vast majority of Filipino population including those living in remote locations. A platform that can easily and cheaply ensure secure contributions and disbursements can materially reduce the time and cost necessary for routine transactions. Mobile-based communications can contribute towards achieving such efficiency though needs to be effectively regulated to ensure secure transactions. Together these processes can be referred to as a delivery system platform.

SSS operations could build upon such an inter-institutional platform to provide efficient and secure coverage for its members, including those in the informal sector. For example, if the current deposits by AlkanSSSya members could be deposited by phone instead of through the savings boxes, it may be possible to substantially scale-up the AlkanSSSya membership.

Further work is also needed to establish mobile money platforms that can support (i) mobile-phone-based remittances from different sources including bank accounts, ATMs, or shops offering money transfer services; (ii) mobile-phone-based account payments or withdrawals; and (iii) phone- or internet-based information inquiries on account balances and entitlements. Mobile money platforms could reduce transaction costs for informal worker participation in social security schemes, improve efficiency for payments and money transfers, and generally remove barriers to savings opportunities for heretofore unbanked individuals and businesses.26

Expanding access to savings can reinforce the agenda of increasing coverage. About one-third of the population over age 15 had bank accounts in 2014 (versus 69 percent for the EAP region), while only about 15 percent had formal savings (versus 36 percent for the EAP region), and only about 4 percent had mobile money accounts.27 The authorities are aware of this and are taking steps aimed at improving financial inclusion.

The DSWD Social Pension plays an important role in ensuring the basic livelihoods of the poorest elderly and broadening its target population would prove more effective in increasing coverage of the elderly when compared with matching grants. The Listahanan national household targeting system could be used as a basis for broadening the eligibility for the Social Pension from the current poor in the bottom two deciles to possibly the poor and near-poor by raising the household eligibility threshold possibly to the bottom four deciles. This would mean that those eligible households in the bottom 40 percent with elderly members over age 65 could qualify for a Social Pension benefit, much in the same way that the same households can qualify for PhilHealth benefits. This would have an immediate impact while the matching grant would take many years to mature.

27 Ibid.
VI. Conclusion

Going forward, additional diagnostic work will be needed to inform the design of specific strategies for improving the coverage and sustainability of social security in the Philippines. For example, a diagnostic evaluation is needed to identify weaknesses in the identification and SSS operations and delivery system, particularly with regard to low-income, informal workers. Contributory pension design options and parameters need to be considered which better align the incentives toward coverage expansion. Beyond the SSS, barriers to savings need to be studied and addressed. Finally, PROST simulations could be supplemented by simulations using additional parameters not yet considered.

This note has looked at some reform options to help the SSS improve sustainability, provide greater incentives to participate, and improve inflation risk coverage. A gradual process of parametric reforms is proposed which does not abruptly or adversely affect existing retirees or workers approaching retirement age. Moreover, it is suggested to weigh the tradeoffs between the objectives of coverage expansion and the potential adverse effect of increases in the contribution rate. Fortunately, the analysis suggests that the SSS scheme can achieve long-term sustainability on a gradual basis with modest changes in the qualifying conditions, benefits, and, possibly the contribution rate.

This note has also suggested options to strengthen social security coverage, particularly of informal workers. These include further strengthening the mechanisms for contributions, account access and payments, and introducing a new SSS savings instrument aligned to the needs of informal sector workers. An assessment of matching contribution subsidies to expand coverage suggested that a more effective alternative would be to broaden the scope of beneficiaries eligible for social pensions.

Improvements in SSS sustainability and the instruments and delivery systems for social security coverage comprise only one part of a broader strategy needed to better protect the vast majority of workers in the Philippines with low, intermittent and variable sources of income. A more systemic view of job creation, labor market and social insurance reforms can help to better protect these workers. Ultimately, the only sustainable approach to combating low-skill, low-wage, and low-security informal jobs is to strengthen the quality of growth and job creation. Measures are needed on numerous fronts to combat the causes of informality, such as removing barriers to competition and growth in real sectors and addressing barriers to formality including taxes and labor market provisions.
References


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