Enrollment of Firms in Social Security in Lao P.D.R.

Perspectives from the Private Sector

The World Bank, November 2010

Enrollment of Firms in Social Security in Lao P.D.R.:

Perspectives from the Private Sector

World Bank, November 2010

Summary

Social Health Insurance (SHI), which is part of a broader social security system, is one of the main risk-protection schemes operating in Lao PDR and is expected to play an important role in moving the country toward universal coverage in the health sector. Although the scheme is mandatory, enrollment among the target population is low due a variety of reasons that are only partially understood. This study was conducted to better understand the factors affecting enrollment in SHI, to document employers' experiences with and perceptions of the scheme, and to identify opportunities and challenges of expanding coverage in the future.

A survey was administered to 130 employers (including 65 member firms and 65 non-member firms) in Vientiane Capital. The results show that the following factors influence enrollment: state-ownership; a mixed foreign-domestic partnership; higher education level of head of company; and being in the trade industry. Explanations for not enrolling in the scheme include the lack of knowledge of the scheme, poor quality of the health care system and infrequent use of health care by employees. Member firms reported on the strengths of the scheme: reduced expenditures for the company, convenience and cost-savings for employees, and improved employee well-being. Weaknesses include: poor value for money, poor quality of care in hospitals, and a poor understanding of the social security benefits and procedures. The study revealed that, in the absence of social security benefits, non-member firms provide few benefits to their employees. Evading social security payments by hiring temporary workers does not appear to be a problem at the moment, but within firms, employees are often given the option to opt-out of the scheme.

The study reveals opportunities for strengthening SHI and expanding enrollment, but also highlights the challenges of achieving high coverage rates. Expansion will require increased formalization of the labor market, effective enforcement mechanisms and effective and efficient tax collection systems. Stronger enforcement also increases incentives for evasion and informality of the labor market, while voluntary enrollment within firms makes the scheme prone to adverse selection. As the government finalizes the new health financing strategy, the costs and benefits of various approaches should be considered. However, regardless of the financing arrangement taken, increased public spending in the health sector and improved coordination across schemes can help to strengthen the health system and build up the foundation on which universal coverage can be achieved.

This note was prepared as part of a World Bank program of analytic work on health financing in Lao PDR, and in collaboration with the London School of Hygiene and Tropical Medicine (LSHTM) and the Social Security Organization (SSO). Core members of the study team included Sarah Alkenbrack (LSHTM) and Magnus Lindelow (WB). The field work was implemented by Indochina Research. Helpful comments on the draft versions of the note were received from Frank Feeley, Kara Hanson, Fiona Howell, Bart Jacobs, Christoff Kurowski, Padeumphone Sonthany, Jean-Marc Thomé and Adam Wagstaff. The team would like to thank the private sector employers for participating in the survey; private sector and government staff (including hospital staff) for participating in key informant interviews; and staff members at the Social Security Organization for their assistance in providing background information. The note summarizes findings from the study; further analysis and details will be disseminated through a separate research report.

Background

Increasing participation in health insurance and risk-protection schemes is a key priority for the Government of Lao PDR. The four main risk-protection schemes operating nationally include: 1) mandatory health insurance for civil servants; 2) mandatory social health insurance (SHI) aimed at private and state-owned enterprises; 3) voluntary community-based health insurance (CBHI) for the informal workforce; and 4) health equity funds (HEFs) for households living in extreme poverty. As the Government of Lao PDR seeks to improve financial protection and access to health care, greater attention is being given to the social security scheme[1] and the role it could play in expanding coverage. However, enrollment in social security - which is mandatory for all enterprises with at least 10 employees (according to a ministerial decree) - has remained low since the scheme's inception. Low enrollment can be attributed, at least in part, to the small scale of the formal sector, limited geographic reach of the scheme (4 provinces only), lack of enforcement and weak regulatory structure, and limited capacity of the Social Security Organization (SSO - the implementing agency for the scheme) to attract new members.

[1] Although the focus of this note is on SHI, the scheme is part of a larger social security program, and therefore the terms "SHI" and "social security" are used interchangeably throughout this document.

Given that expansion of health insurance is a high priority to the Government of Lao PDR, this study was conducted to shed light on the factors affecting enrollment in social security, employers' experiences with and perceptions of the scheme, and benefits provided to employees in firms that do not participate in SSO. Findings from the study will help to identify opportunities and challenges for strengthening the scheme and expanding its reach, and are expected to inform decision-making related to the Government's new health financing strategy that is currently being prepared.[2]

Overview of Social Security in Lao PDR[3]

The social security scheme consists of a comprehensive package of health care and other benefits offered to employees in private and state-owned companies. The package of benefits includes medical care, sick leave, maternity leave, death benefits, employment injury or occupational disease benefits, retirement pensions, life insurance, and disability insurance. Introduced in 1999, the scheme is managed by the Social Security Organization, a semi-autonomous organization within the Ministry of Labor and Social Welfare. Funding for the scheme is generated from a combination of employee and employer contributions.[4] The health care fund, which also receives government subsidies, is the largest of all benefits and finances outpatient and inpatient care, and prescription drugs available at hospitals. There are no co-payments or limits on the number of contacts or services provided. Public providers are paid by capitation, which is fixed at LAK 80,000 (US$ 9.40) per insured person per year [1].

The SSO depends on its public relations department to stimulate enrollment among its target population. The public relations team makes daily newspaper and radio announcements, and also convenes meetings on an ad hoc basis with large companies (100 employees+) to raise awareness about the scheme and encourage enrollment. However, the public relations department is staffed by only five people and lacks the financial resources and capacity to effectively stimulate enrollment among the target population [2].

Overview of SSO legislation defining the target group

According to the SSO Decree 207, the official target group for social security includes all enterprises with 10 or more employees. However, the decree is difficult to enforce for two main reasons. First, Decree 207 is a ministerial decree, and therefore by nature weaker than a law promulgated by the President. Second, no regulatory procedures are in place to enact penalties for non-compliant firms. Although an inspection unit at SSO was introduced in 2008 with a mandate of identifying non-compliant enterprises, at the present time only verbal warnings can be issued. Furthermore, the SSO office is understaffed: like the public relations department, the inspection unit is staffed by only 5 employees.

As a step to strengthening the regulatory framework around social security, the SSO is drafting guidelines for inspections and sanctions for non-compliant companies, and is also working with other line ministers to promulgate a law specific to social security. The new law will mandate enrollment of all enterprises *with at least one employee*.[2] Although the Labor Law (2006) mandates that *"all labour units must participate in…social security"*, the language is vague in that it does not specifically define the term "labor unit" or the minimum number of employees that constitute a "unit"[3].

Overview of the current target group

While the official target group includes all enterprises with at least ten (and eventually one) employees, the SSO currently targets only a small subset of enterprises in the country. This is due to the way in which the SSO collects information about its target group, which involves obtaining a list of businesses that are registered with the central or provincial Tax Registration Office (Ministry of Finance) and storing information about these businesses in a database. The database includes a total of 1,357 businesses, all of which are located in the four provinces where the scheme is running (Vientiane Capital, Vientiane Province, Savannakhet and Khammoune). The majority of this group (99%) consists of firms with 10 or more employees. However, because the database includes only companies that pay taxes to the Tax Registration Office, enterprises that do not have a tax identification number are excluded from the target group.

---

[2] The study was designed and carried out by a team of researchers from the World Bank and London School of Hygiene and Tropical Medicine (LSHTM). A local research team was hired to carry out data collection under the supervision of the World Bank/LSHTM team. The study was funded by the World Bank. Implementation of the survey was approved by the SSO and ethical approval was granted by the National Institute of Public Health in Laos and LSHTM in the United Kingdom.

[3] Much of the information presented here was gathered through key informant interviews with stakeholders within the SSO, document review and secondary data analysis.

[4] Employees and employers contribute 4.5 per cent and 5 percent of employees' salaries, respectively, up to an income ceiling of LAK 1,500,000. Health insurance makes up the largest fund, comprising 4.4 out of 9.5 percentage points of an employee's earnings.

In order to provide some perspective of the size of the current SSO target group relative to the universe of enterprises operating in the country, we performed secondary data analysis using the Lao Economic Census [4] – a survey that summarizes information about all economic units[5] operating in the country.

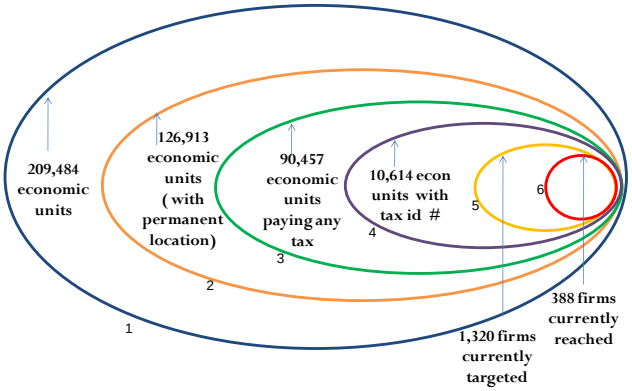
The findings, summarized in Figure 1, are helpful for understanding various options for expanding the SSO target group in the future. The first (outer) ring represents all 209,484 economic units that operated in the country at the time of the economic census (2006), many of which had no permanent address or were located in communities without road access. These units, which are usually considered part of the informal sector[6], include mobile shops, street vendors, lottery sellers, tuk tuk drivers, and other temporary shops. The outer ring also includes international organizations and civil servants, neither of which are considered part of the private sector, and are therefore not targeted by the SSO.

When we exclude informal economic units, international organizations and civil servants, we are left with 126,913 economic units (represented by the second ring).[7] However, even though economic units in this category have a permanent location, the degree of formality with which they operate varies. For example, only 40% of businesses in this category hold a trade registration certificate, while only 71% hold a tax registration certificate.[8] In identifying opportunities to expand SSO, it is clear that targeting businesses that are not yet tax registered would present a challenge.

The third ring represents the 90,457 units that are paying some form of tax. Clearly, the fact that businesses are paying taxes indicates that they have a somewhat formal structure. However, even among this group, there are varying degrees of formality. Depending on the accounting system, businesses make their tax payments using one of three methods: a lump sum tax or daily tax (for firms with less advanced accounting practices), or tax paid to the Tax Registration Office on a regular basis using a tax identification number. According to the Lao Economic Census, firms with a tax identification number account for only 8% of economic units in the country (represented by the fourth ring). Thus, by targeting only firms with a tax identification number, the SSO automatically misses an opportunity to target the other 92% of enterprises in the country.

The SSO database of target firms comprises 1,320 enterprises (the fifth ring).[9] However, due to low compliance, only 388 enterprises were enrolled in social security in January 2009 (the sixth ring). These 388 companies represent only 29% of companies in the SSO's database of target firms, but because most enrolled firms are large, this group accounts for 61% of targeted employees. Collectively these 388 companies provide insurance for 46,731 employees, and 86,690 beneficiaries[10]– approximately 1.5% of the Lao population.[5]

Figure 1. *Economic units operating in Lao PDR*



Source: Compiled by the authors using data from Lao Economic Census (2005/6) and SSO Database.

While the above diagram does not give an indication of the proportion of the *population* that could potentially be covered (see estimated scenarios presented in Appendix 2), the data indicate that there is considerable opportunity to

[5] An economic unit is defined as any business entity, either formal or informal, including shops that operate any economic activities. This group also includes non-profit and non-government organizations but excludes international organizations.

[6] The line between the informal and formal sector is often blurred. The informal sector usually refers to unregistered production units that are owned and operated by individuals, and sometimes unpaid family members.

[7] This group is likely an overestimate of the number of enterprises in the country, given that each branch office of a single company is counted as a separate economic unit. However, based on the Lao Economic Census, 99% of the economic units are solely owned (not belonging to any other enterprise).

[8] While the majority of economic units that do not have a tax registration certificate are very small (with less than five employees), 370 of these firms are medium-sized (10 to 99 employees).

[9] The SSO target group is much smaller than the group of tax-registered firms, in part because the SSO targets only firms with 10 or more employees and in 3 provinces only.

[10] The updated figure for number of beneficiaries at the end of 2009 was 93,086 (MOH monitoring data, 2009).

expand the *number of firms* that could be reached, at least in principle.

Overview of Study

Key policy questions

Prior to designing the study, we conducted key informant interviews with government staff, leaders of business associations (also known as membership organizations), and hospital staff. Through these discussions, the following key policy questions to be addressed by the study were identified:

Enrollment

- Which employer characteristics are associated with enrollment in social security? (i.e. size of firm, type of ownership, risk profile, etc.) ?
- What motivates employers to enroll/not enroll in social security?
- Do firms intend to enroll/maintain enrollment in social security in the future?

Experiences

- What has been the impact of social security on business?
- What are the strengths and weaknesses of the social security scheme?
- Is the benefit package offered by non-SSO-member firms comparable to social security benefits?
- Are member firms employing strategies to evade social security contributions?

Study Approach

To answer these questions, a structured questionnaire was administered to 130 employers (including 65 member firms and 65 non-member firms), interviewing heads of companies where possible.[11] The sample was randomly selected from the four biggest industries in the SSO target group: manufacturing; construction; trade; and services, using strata that corresponded to industry and number of employees, with firms being selected from the SSO database. The survey restricted attention to Vientiane Capital.

Given the objectives of the study, the questionnaire was designed to capture variables that are expected to influence enrollment, such as characteristics of businesses (ownership, company size, revenues, etc.), sociodemographics of company leaders, and exposure to social security. It included both open- and closed-ended questions. The survey also collected details regarding employment contracts, employee benefits, and employers' perceptions of the scheme.

As is often the case with firm surveys, the refusal rate was moderately high, but this was expected given the difficulty of interviewing private sector employers.[12] The firms that refused to participate differed between the enrolled and unenrolled populations: in the SSO group, mostly larger firms (>50 employees) refused to participate while in the non-enrolled group mainly smaller firms (<50 employees) refused to participate. These differences between groups may lead to some concern of sampling bias. The sample was weighted to adjust for the refusal rates and the firms that were no longer in operation or could not be found. Thus, the results can only draw conclusions about the SSO's target group of firms that are presently in business.

Findings

Enrollment in Social Security

Background Characteristics of Sample

The table in Appendix 1 outlines the relative similarities and differences between SSO member and non-SSO member firms in the sample, with respect to a variety of background characteristics. Significantly more SSO member firms are state-owned, under foreign ownership, and have a larger workforce and higher revenues. SSO firms also employ fewer permanent workers (relative to the size of their workforce) than non-member firms. However, it is

[11] Pilot-testing took place in February 2009. Field work was conducted by a local research team from March through May 2009. Thirty-nine percent of interviews were conducted with the head of the company (e.g. director, general manager, chief executive officer, etc.); 30% were conducted with the head accountant; and 33% were conducted with the human resources manager. (Some were conducted with more than one respondent). Given that the study focused on benefits and contracts it was reasonable for the head accountant or human resources director to participate when the head of the company was not available.

[12] The response rate was between 67% and 80%. The former rate includes contacted firms in which nobody was available to be interviewed or a follow-up appointment could not be made in the study period. The latter rate includes only firms that explicitly refused to participate. Interviewers attempted to schedule an interview three times before randomly selecting another enterprise. It is important to note that one third of the firms that were identified as eligible had either closed or could not be found (e.g. the number was disconnected or the business was no longer at the stated location), indicating the poor quality of the database used by SSO. (These firms are not factored into the response rate.)

important to note that differences noted here are simply differences in the sample: further analysis using multivariate logistic regression allows us to examine differences in key variables while holding all other factors constant. These findings are presented as odds ratios below.

Which employer characteristics are associated with enrollment in social security?

The odds ratios presented in Table 1 compare the odds of enrolling in social security for companies with and without certain characteristics. The odds ratios represent the strength of the relationship between the variable of interest and enrollment in social security when all other variables are held constant.[13] An odds ratio greater than one represents a greater likelihood of enrolling, relative to the reference group, while an odds ratio of less than one represents a lower likelihood of enrolling, relative to the reference group. Given the small sample size, we consider a p-value of less than 10% to be significant. The findings show that companies whose heads have a university education are more than three times more likely to enroll in social security, over companies whose leaders have less than a university education. The odds of enrolling are also significantly higher for firms in the trade industry relative to the services industry.

Ownership was found to be associated with enrollment. The odds of enrolling are approximately 23 times higher for state-owned enterprises than for private firms, which is not surprising given that social security is a government-mandated program.[14] Although foreign-owned companies are not significantly more likely to enroll, mixed companies

Table 1. *Odds ratios of enrollment, by firm characteristic*

	Odds Ratio	95% Confidence Interval		p
Head of company has a university education	**3.475**	**1.188**	**10.162**	*****
Head of company is male	**0.627**	**0.177**	**2.217**	**-**
Industry type (Reference group: services)				
Manufacturing	**1.210**	**0.289**	**5.056**	**-**
Construction	**0.320**	**0.038**	**2.698**	**-**
Trade	**3.697**	**0.845**	**16.171**	**(*)**
Ownership 1: State-owned or partially state-owned (ref: 100% private)	**23.134**	**1.987**	**269.364**	*****
Ownership 2: (Reference group: 100% domestic)				
100% foreign (vs. domestic)	**6.174**	**0.319**	**119.270**	**-**
mixed (vs. domestic)	**20.282**	**2.965**	**138.751**	*****
More than one service outlet/branch/factor/store	**1.505**	**0.421**	**5.375**	**-**
Revenues (Reference group: <1 billion kip)				
1-10 billion Kip	**1.342**	**0.443**	**4.071**	**-**
> 10 billion Kip	**1.300**	**0.299**	**5.657**	**-**
Member of business organization (ref: no membership)	**2.064**	**0.728**	**5.857**	**-**
Firm has higher than avg perceived risk (3+ on a scale of 1-5)	**0.707**	**0.102**	**4.910**	**-**
Size of permanent workforce =20-59 employees (ref: 0-19 emp)	**1.998**	**0.568**	**7.026**	**-**
Size of permanent workforce = 60+ employees (ref: 0-19 emp)	**3.550**	**0.815**	**15.456**	**(*)**
Employs any temporary workers	**1.202**	**0.388**	**3.726**	**-**
At least 10% employee turnover (annually)	**0.522**	**0.159**	**1.711**	**-**
Taxes paid at central level (ref: taxes paid at lower levels)	0.675	0.160	2.848	-

**significant at the 5% level (*) significant at the 10% level. A p-value is a statistical term that measures the likelihood that a difference observed in the sample is due to chance. A result that is significant at the 5% level has a p-value of less than .05. The confidence interval indicates the reliability of the estimated odds ratio. A 95% confidence interval means that there is a 95% chance that the true estimate falls within the interval. Because the sample is small, p-values that are less than .10 are accepted as (borderline) significant.*

[13] Given the cross-sectional nature of the data, the associations observed here do not imply causal relationships.

[14] In this sample, all but one state-owned or partially state-owned company are enrolled in social security. Therefore, the effect of state-ownership on enrollment is very strong. It is not clear whether there is an additional mechanism for SOEs to enroll in social security. For example, it is possible that SOEs are pressured to enroll or are automatically enrolled. Whether or not this is the case will require further investigation.

(in which ownership is shared between domestic and foreign owners) are 20 times more likely to enroll in social security than domestic companies. It is possible that mixed companies, due to the nature of their business, receive pressure to comply with industry regulations, or that these types of firms have a stronger compliance culture.

Prior to the interviews, key informants reported that they expected enrollment to be higher for larger firms. The study confirmed that larger firms are more likely to enroll, all other factors being equal. However, a firm's decision to enroll is not significantly influenced by a firm's perceived risk, employee turnover, or financial status. Although key informants expected pressure from leaders of membership organizations to influence employers to enroll in SSO, this claim was not supported by the study findings.

What motivates employers to enroll/not enroll in social security?

To better understand employers' decisions to enroll, employers were asked to rate a number of possible reasons for enrollment/ non-enrollment on a scale of 1 to 5, with 1 being not at all important and 5 being very important.[15] The results, summarized in Table 2, confirm the trends identified through multivariate analysis but also shed further light on employers' decision-making process. Among the insured, the most important reason for enrollment was to ensure employees are covered with health insurance. Increasing employee satisfaction, and improving the health and well-being of employees were also important factors. These two findings indicate that employers are most concerned with the health insurance benefits within the social security scheme. However, retirement benefits are also relatively important.[16] The finding that pressure from the SSO was not an important factor was not surprising given that SSO is not currently enforcing enrollment.

Among the non-enrolled cohort of the sample, the most important reason for non-enrollment was that the company's benefit package is superior to social security – an interesting finding given that few companies offer health insurance or other benefits to their employees, as shown in the next section of the report. Therefore the only possible explanation of this finding is that although non-enrolled firms offer fewer benefits to their employees, the benefits they do offer are of higher quality than those offered through by the SSO. However, it is more likely that in their explanations of why they were not enrolled, employers tried to justify their behavior in terms that did not make them look bad. Other important reasons for not enrolling were: employers' lack of knowledge of social security, the poor quality of government hospitals, and the fact that employees do not use benefits or do not get sick.

To better understand the process by which a firm decides to enroll in social security, employers were asked to identify the people in charge of making the decision to enroll. Most firms mentioned that the director of the company, the general manager or the owner, and less often the executive board, make the decision to enroll. In a few companies, the personnel manager and all staff members are involved in the decision process.

Table 2. *Most important reasons for enrollment/ non-enrollment*

Reasons for enrollment	Rating (1-5)
To ensure employees have health care coverage	4.28
To increase employee satisfaction	4.11
To improve health and well-being of employees	4.08
To ensure employees have retirement benefits	4.00
Strong pressure from international bodies	3.05
Strong pressure from SSO	2.74
Strong pressure from employees	2.72
Strong pressure from membership organization	2.71
Reasons for non-enrollment	**Rating (1-5)**
Company benefits are better than SSO benefits	4.11
Do not know much about social security	3.42
Quality of government hospitals not good	3.22
Do not use health care benefits/ staff do not get sick	3.22
Employees do not want SSO	3.12
Cost of SSO is too high	2.97
Do not trust that money is used well	2.83
High turnover among employees	2.57
Many temporary employees	2.38
Employees prefer to purchase private insurance	2.35

Do firms intend to enroll/maintain enrollment in SSO in the future?

The study found that almost all SSO member firms (95%) intend to be enrolled in the scheme in 3 years, compared with 38% of non-member firms (51% are unsure and 11% said they do not intend to be enrolled). The majority of firms that are "unsure" about enrollment or do not intend to enroll are domestic, privately owned businesses. Promotion activities targeted at leaders of this type of firm

[15] The possible factors affecting enrollment/non-enrollment were identified by first asking employers to list their most important reasons for enrolling/not enrolling. Respondents were then asked to rank the full list of responses.

[16] In a survey question, respondents ranked health care as the most important benefit, followed by retirement benefits and sick leave.

– e.g. face-to-face meetings to discuss SSO and answer questions about the scheme – could help encourage enrollment. Currently, only 13% of non-enrolled firms in the sample have ever attended a meeting where SSO was promoted.

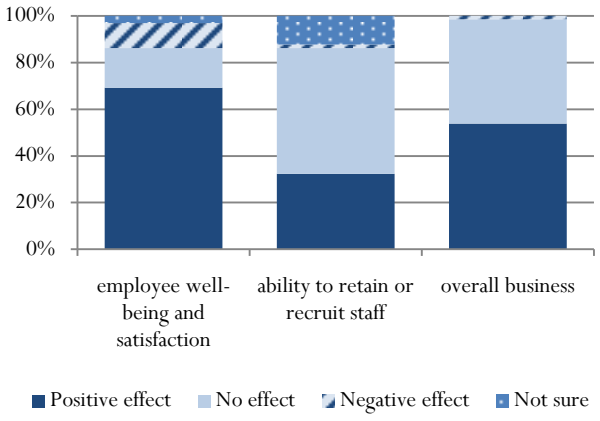
Experiences with social security

What has been the impact of social security on business?

As shown in Figure 2, the majority of respondents (69%) stated that social security has had a positive effect on employee well-being and satisfaction. However, most feel that the scheme has had no effect on the ability to retain staff or recruit staff members. Employers explained that while some prospective employees inquire about benefits prior to accepting a position, most job-seekers are mainly concerned with salary.

Although 54% of SSO-enrolled employers claim that the impact on overall business has been positive, almost half say there has been no effect. Among firms reporting a positive effect, employers explained that social security: a) gives firms a competitive advantage over non-enrolled firms because it decreases company expenditures; b) helps to build trust with staff members; and c) increases productivity of employees. However, other employers noted that being enrolled in social security *decreases* revenues unnecessarily because the cost of contributions exceeds the benefits used by employees.

Figure 2. *Impact of Social Security on Business*



What are the strengths and weaknesses of the social security scheme?

Employers who are currently enrolled in social security were asked to comment on the strengths and weaknesses of the scheme. The three most common responses are described below.

Strengths

Social security reduces employers' expenditures on benefits for which the company would otherwise pay.

Social security provides convenience and cost-savings to employees, in that employees can use cards for hospital care, rather than paying cash.

Being enrolled in social security improves employee well-being. Employers report that SSO gives employees a sense of "security", "warm feelings", "trust", and "confidence" and "increases employee satisfaction". According to one employer, higher employee satisfaction due to SSO benefits translates into higher productivity.

Weaknesses

Employers do not perceive the scheme to be of good value, either because the staff do not use benefits (most respondents made specific reference to not using health care benefits) or because contributions exceed the benefits used. Employers are particularly concerned that health insurance does not cover check-ups and feel that including free check-ups would improve the value of the scheme.

Quality of care at hospitals is poor, according to SSO members - and worse for social security members. For example, SSO employers report that their employers experience longer waiting times, are treated poorly by health care professionals, and receive drugs of inferior quality, relative to non-members. One respondent mentioned that because of the long waiting times and poor quality *"…members sometimes have to go to the private clinic for treatment."*

Communication by SSO regarding benefit structure and the procedures associated with the scheme is poor. Members reportedly have very little contact with SSO staff and therefore no opportunity to learn more about SHI. Some SSO representatives do not clearly explain the details of the scheme. Moreover, there are reports that SSO staff members are unfriendly when providing information to members or prospective members.

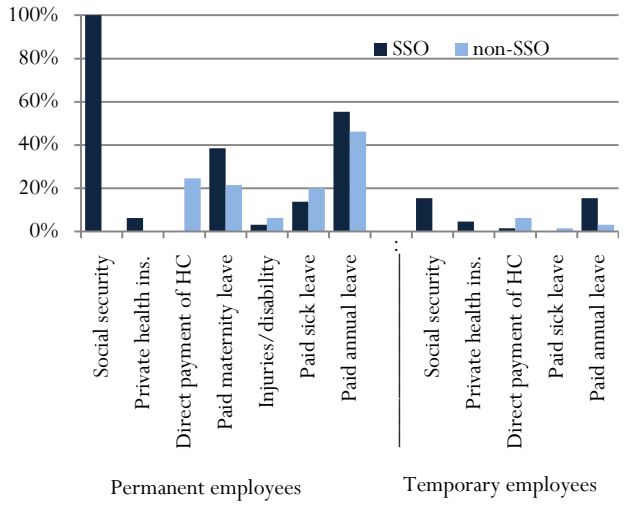
Other less frequently reported complaints of the scheme include slow and cumbersome documentation processes required to submit health care claims and the difficulty of using (or switching) hospitals for the primary source of treatment.

Is the benefit package offered by non-member firms comparable to social security benefits?

As stated earlier, the most important reason for not enrolling in social security is that employers offer a better package of benefits than that offered by the SSO. However, the study findings show that the non-enrolled firms offer far fewer benefits to their employees than do SSO member firms (See Figure 3). In fact, the majority of non-enrolled employers do not offer health care benefits: only one quarter of non-SSO firms make direct payments for employees' health care, while none have private insurance. In contrast, some SSO member firms offer extra insurance for programs that are already included in the social security package (e.g. private health insurance, maternity benefits, coverage for injuries, and sick leave).

Although private insurance is not commonly offered at the firm level, it is possible that *employees* in non-SSO member firms are purchasing private insurance at the household level. Key informant discussions found that AGL, and to a lesser extent, Toko Assurance, are the two players in the private insurance market in Lao PDR and plans are underway for rapid expansion. AGL has launched new initiatives, including cooperative arrangements with International NGOs and villager groups, whereby premiums are financed by income generating activities. AGL offers a benefit package for as low as US$ 2.50 per month and covers care both within and outside Lao PDR [6].

Figure 3. *Benefits offered to SSO and non-SSO employees*



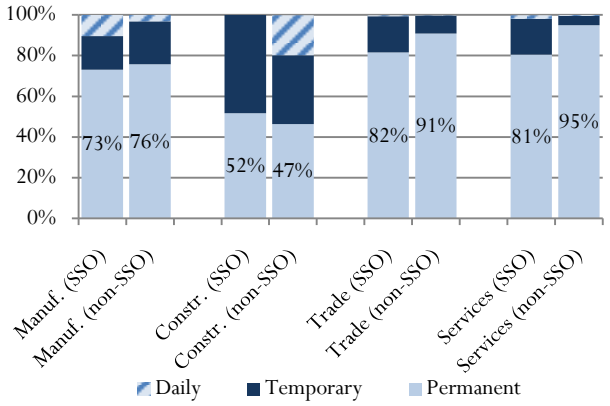
With respect to temporary employees, very few in either group receive employee benefits. However, 15% of SSO firms do extend social security and pay annual leave to their temporary employees. According to employers, the length of time an employee can work as a temporary employee varies across firms, and 30% of firms report that there is no limit. Because the majority of temporary employees do not receive benefits, there may be a financial incentive for employers to hire temporary employees to fulfill the duties of permanent employees. The potential for such evasion is discussed in the next section.

Are member firms employing strategies to evade social security contributions?

One of the challenges of implementing and enforcing mandatory insurance is evasion of contributions. For example, the international body of literature on social security describes the ways in which many enterprises fail to comply with social security (e.g. by underreporting the number of permanent employees, reclassifying job descriptions - in order to hire temporary workers instead of permanent, underreporting earnings, and failing to remit employee contributions) [7-9]. In Lao PDR, it was expected that any evasion of social security payments would be minimal, given that penalties are not yet enacted for non-compliance.

One way to detect invasion is to examine the structure of the workforce. A disproportionately high number of temporary workers could indicate that a firm is trying to evade social security contributions. The study found that overall, enrolled firms employ more temporary and daily workers than non-enrolled firms (24% vs. 15%; the differences are significant at the 10% level, as shown in Appendix 1). However, when we control for type of industry (See Figure 4), the difference in the proportion of non-permanent workers between SSO and non-SSO firms is very small and is not statistically significant. Furthermore, when controlling for differences in size of workforce, revenue, and ownership (private vs. state-owned; foreign vs. domestic), the differences almost disappear. It seems that SSO firms are no more likely to employ temporary workers than non-SSO member firms and that the extent to which firms hire temporary workers is likely related to the nature of the business. For example, construction companies tend to hire workers on a seasonal basis, explaining the higher proportion of temporary workers in the construction industry.

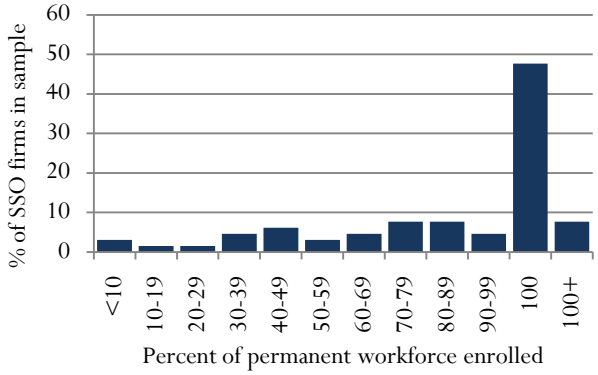
Figure 4. *Composition of workforce by industry and SSO status*



Given that enrollment is not enforced, it makes sense that member firms are no more likely to evade payments than are non-member firms. However, it is possible that, regardless of enrollment, firms are evading payment of benefits in general. The language in the Labor Law is such that even employers without social security are required to provide sick leave, maternity benefits, health care, occupational disease benefits, and pensions. These expenses must be borne by the employer for firms that do not have social security. Therefore, it is possible that firms (both SSO and non-SSO members) hire temporary workers, or under-report number of permanent employees as a way of avoiding these payments. For example, key informant discussions with the SSO revealed that after enrolling with the SSO, some companies reported gradual declines in the size of their permanent workforce. However, according to SSO staff, random checks by their organization revealed that in some of these firms the size of the permanent workforce had not actually decreased but that the firm had instead underreported the number of employees [2]. Underreporting the number of employees is a well-known evasion tactic for reducing social security payments [8], and may become a growing concern in Lao PDR if SSO strengthens enforcement. Stronger regulation could create incentives for employers to not only evade social security payments by under-reporting employees but could also lead to a growth in the informal sector (because firms wishing to evade contributions will fail to register some or all of its workers). A rise in informality also decreases the tax base for general revenues [8, 10].

Prior to the study, key informant interviews suggested that some employers allow employees to opt-out of social security. Given that social security is mandatory for all permanent employees, opt-outs can be considered an evasion strategy used to reduce costs of providing benefits. To further investigate the extent to which opt-outs take place, researchers compared data on the number of permanent workers in the company with the number of employees enrolled in social security for the same time period. If firms are complying with social security, 100% of the permanent workforce should be enrolled. However, the findings presented in Figure 5 show that 44% of member firms enrolled less than 100% of the permanent workforce in the scheme. In fact, 94% of employers with social security benefits openly admitted to giving employees the option to enroll. Voluntary enrollment within firms poses a challenge to expansion of social security because it decreases revenues to the SSO. Voluntary enrollment also encourages healthy and lower-risk individuals to leave the risk pool. This phenomenon of adverse selection could ultimately threaten sustainability and effectiveness of risk-pooling.

Figure 5. *Percent of permanent workforce enrolled with SSO*



**Firms that offer SS benefits to both permanent and temporary employees are effectively enrolling more than 100% of their permanent workforce.*

Looking forward: Challenges and Opportunities

This study brings to light a greater understanding of employers' attitudes toward social security. Although there are limitations to the study[17], the results are nonetheless helpful for understanding perspectives of the private sector – a group that is not usually engaged in health sector reform discussions. A number of issues also emerge from the study, which point to the following operational changes that could strengthen the scheme and facilitate expansion:

[17] The narrow sampling frame limits the generalizability of the findings; the high refusal rate and the use of different respondents (e.g. head of company, HR director) may bias the responses; the small sample leads to large variation in estimates and large confidence intervals, which can increase the likelihood of sampling errors.

- *Improve awareness-raising, promotion and communication.* Awareness-raising activities and face-to-face meetings with employers from privately-owned domestic firms – the least likely to enroll – could be effective strategies for bolstering enrollment rates. However, new approaches will be required to reach smaller firms with less formal structures. For example, large hotels that have been enrolled in social security for several years have begun to realize the benefits to their bottom line (i.e. because they do not have to cover direct payments of health care and sick leave) and are now working with the Lao Hotel and Restaurant Association to encourage smaller guest houses to join the scheme [11]. Similar partnerships may be feasible in other sectors.

  Employers of SSO-member firms complain about the content, frequency and style of communication by SSO (e.g. SSO members reported that SSO staff are not well-informed about the scheme and also treat SSO members poorly). Strengthening communication skills and increasing communication channels between the SSO and businesses could therefore help to improve satisfaction among members, and could ultimately attract new members.

- *Promote improvement in quality of health services.* Poor quality of care in government hospitals is a major reason that employers do not enroll in social security. Thus, quality improvements to the system as a whole would have a positive impact on enrollment. Although quality improvement is a complex issue requiring multifaceted interventions, there is nonetheless potential for the SSO to influence service delivery by using its purchasing power to encourage better quality care. For example, the SSO could make a percentage of its capitation payment contingent on quality of services, or issue penalties to staff members who treat patients poorly.

- *Make the social security package, as a whole, more attractive.* Although SHI is the largest and most important benefit within the social security package, it is important to note that enrollment in SHI is linked to the broader package of social security benefits and that decisions to enroll in health insurance are therefore determined by the perception of the benefit package as a whole [12]. For example, if retirement benefits (the second most important benefit in the scheme) are not financially attractive to workers, employers may be discouraged from enrolling in social security. A study in Vietnam found that a private sector worker with less than 20 years left before retirement is better off saving for himself than making contributions to the social security scheme. For those with more than 20 years left until retirement, it makes sense to contribute only for 30 years in total.[12] The results from Vietnam indicate that reforming pensions, and possibly other benefits, will make social security more attractive to private sector employers and may facilitate the scheme's expansion. The same could be true for Lao PDR, although to be sure, further research along the lines of the Vietnam analysis could be undertaken.

In addition to the findings generated from the study directly, the descriptive analysis of the social security scheme (in the background section of this report) highlights several challenges to the scheme. With these challenges in mind, the following operational changes are proposed:

- *Introduce legislation to enforce enrollment.* The scheme is effectively voluntary at present (for firms, and also for employees within firms). Although inspections have begun, the SSO will be in no position to penalize non-compliant firms until a law is enacted. Completion of the guidelines for inspections, which will be drafted in the near future, will also be important for strengthening enforcement but without a law, inspections and sanctions will carry little weight.

- *Build capacity of SSO office*. Efforts to increase promotion or strengthen enforcement will require expansion of various departments (e.g. the inspections department; the public relations department) and capacity building. Given the poor image of SSO, public information and customer service training will be critical for SSO. However, it may be beneficial to contract-in certain tasks such as the development of public information strategies and independent customer feedback surveys.

- *Expand target group.* As the SSO looks to increase coverage of social security in the future, there are several possible routes it could consider. These include: 1) expansion within the current target group; 2) expansion to new geographic areas; 3) expansion to smaller enterprises; and 4) expansion of the target group beyond the narrow group of tax-paying firms. To get an estimate of the population that could realistically be reached, scenarios were developed using various assumptions. These scenarios are described in detail in Appendix 2. The second scenario shows that even if compliance among the current target population increases to 80% of beneficiaries, increased enrollment would result in a coverage rate that – on a population level – is not substantially different from

the current coverage rate. If the target group were expanded to "hard-to-reach" groups (e.g. firms with less than 10 employees, firms without a tax identification number, firms not paying any tax), coverage rates would still remain relatively low because because compliance for less formal and smaller firms would be difficult to enforce, and because smaller firms do not add substantially more employees. Although the cost estimates of the scenarios are not included, it is likely that expansion of the target group to these "hard-to-reach" groups will result in diminishing returns. Moreover, any increase in coverage of the current scheme is likely to reach the better off, and is unlikely to help the country achieve broader goals of improved equity and poverty reduction.

- *Improve tax registration.* Given the small number of firms with a tax identification number (8%), monitoring tax payments will remain a challenge, even if enforcement is enhanced. One way to address this challenge would be to bring more firms into the formal tax system – e.g. by linking tax and business registration more clearly. Furthermore, as noted in the World Bank's survey of "Doing Business in Laos", there are various bottlenecks of the business registration process that could be simplified, thereby making it easier to monitor payments [13],

- *Consolidate administration to enhance administrative efficiency.* In the long run it may be more efficient to collect and enforce SHI premiums and other contributions through a single agency (e.g. the tax office, Ministry of Finance), rather than through the SSO. This approach has been used in Argentina and is expected to facilitate compliance because employers and workers need make payments only to a single agency rather than to multiple agencies [8]. However, the advantages and disadvantages of combining collection in Lao PDR would have to be analyzed further.

  Establishing new reporting procedures could also help to minimize evasion. For example, in Ukraine, a new reporting procedure requires employers to indicate the names of employees for whom the social security contributions are being made. This system helps to identify employers that do not contribute for each employee[8]. However, a certain level of sophistication in enforcement is required.

But while these operational changes can strengthen SHI and expand enrollment among the target population, other challenges may be more difficult to overcome. First, there are high costs to stronger enforcement, as offices will need to be established throughout the country (currently only one national office and two provincial offices exist) and infrastructure and legislation required for enforcement will need to be developed. The costs would likely increase considerably once smaller and less formal firms are targeted. Furthermore, stricter enforcement can exacerbate incentives for informality and evasion, the costs of which can be significent [10]. For instance, in Colombia, evasion of social security payments among formal sector workers was estimated to cost US$836 million in forgone revenues in a year (2.75% of GDP),[14] while in the Philippines and Kazakhstan, 30% and 40% of expected revenues, respectively, were actually collected[15, 16].

Apart from the costs relating to enforcement and evasion, SHI also has other implications that need to be considered. Adverse selection – which is present in the Lao scheme – can lead to cost escalation by increasing the average cost of health care per member. The scheme may be forced to raise contributions to cover the costs, leading to further evasion, or look to general tax revenues to cover the deficit. Strengthening enforcement within and across firms could help to reduce adverse selection but would not eliminate it. A universal coverage scheme on the other hand, would eliminate adverse selection by enrolling the entire population, but would of course bring other challenges [12].

From the synthesis of the issues highlighted by this study, it is clear that although the social security system can play an important social insurance role for the small but growing formal sector, it is unlikely to be a vehicle for improving access to health services, reducing health-related financial risk on a broad basis, or generating substantial revenues for the health sector. To achieve these goals, complementary approaches will be needed. There is scope for building on other health protection schemes, including community-based health insurance and health equity funds. Currently, the different health protection schemes are highly fragmented. However, the new health financing strategy envisages that the schemes will be merged over the next few years [17]. This would be an important step towards improved coordination and reduced administrative costs. Integration under one organization could also increase purchasing power and facilitate better supervision of quality. However, given the current low coverage rates it is unlikely that simply merging the schemes will facilitate expansion of enrollment.

To address the challenge of low coverage, substantial government (or donor) financing will be required.

Currently, government spending on health in Lao PDR is very low by international standards, but fiscal space is set to increase in coming years due to growing natural resource revenues and improved tax administration. Insofar as the government opts to use this space to increase spending on health, these funds could be used to either subsidize health insurance coverage directly, or increase funding to health care providers (potentially based on volume or other measures of performance) and reduce the charges for patients. Both options can contribute to improved access and financial protection, and both have advantages and disadvantages. These issues need to be studied and discussed in more detail and the benefits and trade-offs of achieving universal coverage through different modes of financing need to be reviewed.

Although the recommendations from this study do not provide a prescriptive plan for the way forward, they do provide a platform for dialogue during the development of the health financing strategy. As the government sets forth a strategy for health financing reform, it will be critical to base plans for the future on a realistic assessment of what can be achieved through current health protection schemes, and to be clear on the government expenditure commitments that are needed to achieve health sector objectives.

References

1. Thomé, J.-M. and S. Pholsena, *Chapter III: Lao People's Democratic Republic: Health Financing Reform and Challenges in Expanding the Current Social Protection Schemes*, in *Promoting Sustainable Strategies to Improve Access to Health Care in the Asian and Pacific Region*. 2009, UNESCAP.
2. Personal communication with Social Security Office. December 17, 2008: Vientiane, Laos.
3. President of the Lao People's Democratic Republic, *Labour Law*, P.s. office, Editor. 2006, National Assembly: Vientiane.
4. National Statistics Center, *Lao Economic Census*. 2005/2006.
5. Social Security Office, *Database on enrolled firms*. 2008.
6. Personal communication with AGL and Toko. 2009.
7. McGillivray, W., *Contribution evasion: Implications for social security pension schemes.* International Social Security Review, 2001. **54**(4): p. 3.
8. Bailey, C. and J. Turner, *Strategies to Reduce Contribution Evasion in Social Security Financing.* World Development, 2001. **29**(2): p. 385-393.
9. Wagstaff, A., *Social Health Insurance vs. Tax-Financed Health Systems - Evidence from the OECD*, in *Policy Research Working Paper #4821*. January 2009, The World Bank: Washington, DC.
10. Wagstaff, A., *Social health insurance reexamined.* Health Econ, 2010. **19**(5): p. 503-17.
11. Personal communication with Lao Hotel and Restaurant Association. June 2008.
12. Lieberman, S.S. and A. Wagstaff, *Health Financing and Delivery in Vietnam: Looking Forward*. 2009, Washington, DC: The International Bank for Reconstruction and Development/ The World Bank. 171.
13. The World Bank, *Doing Business 2010: Lao PDR*. 2009, The World Bank and International Finance Corporation.
14. Escobar, M.-L. and P. Panopoulou, *Chapter 22. Health*, in *Colombia: The Economic Foundation of Peace*, M. Giugale, O. Lafourcade, and C. Luff, Editors. 2003, World Bank: Washington, DC. p. 653-707.
15. Jowett, M. and W.C. Hsiao, *The Philippines: Extending Coverage beyond the Formal Sector*, in *Social Health Insurance for Developing Nations*, W. Hsiao and R.P. Shaw, Editors. 2007, The World Bank: Washington, DC. p. 81-104.
16. Gottret, P. and G. Schieber, *Health Financing Revisited: A Practitioner's Guide*. 2006, Washington, DC: World Bank.
17. MOH Lao PDR (Department of Planning and Finance), *Draft Health Financing Strategy, Lao PDR, 2011-2015*: Vientiane, Laos.

Appendix 1. *Background characteristics of sample*

Firm Characteristics	**SSO (n=65)**	**Non-SSO (n=65)**	**Difference**
Industry category			
Manufacturing	30.8%	33.8%	n/a
Construction	9.2%	6.2%	
Trade	20%	24.6%	
Services	40%	35.4%	
	100%	*100%*	
Ownership (private/state)			
Ownership 1: State-owned or partially state-owned (0=100% private)	26.2%	1.5%	0.001*
Ownership 2:			
100% domestic	39(60%)	54(83.1%)	0.005*
100% foreign	14(21.5%)	9(13.9%)	
Mixed partnership (domestic & foreign)	12(18.5%)	2(3.1%)	
Total	*65(100%)*	*65(100%)*	
Employees			
Mean # of permanent employees	80.5	63	0.461
Mean # of temp employees	36.9	7.5	0.024*
Mean # of daily wage employees	4.6	0.9	0.178
Permanent employees as a % of workforce	75.8%	84.5%	0.094**
% of workforce female	37.4%	41.1%	0.408
Size of company (financial)			
Company Assets			
< 1 billion kip	27.7%	40.0%	0.130
1-10 billion kip	41.5%	43.1%	
> 10 billion kip	30.8%	16.9%	
Company Revenues			
< 1 billion kip	29.2%	49.2%	0.012*
1-10 billion kip	41.5%	40%	
> 10 billion kip	29.2%	10.8%	
Other firm characteristics			
>1 service outlet/factor/branch/store	78.5%	76.9%	1.000
Member of business organization	56.9%	36.9%	0.035*
Higher than average risk	16.9%	13.9%	0.627
Age distribution (at least 50% of employees are <35 years)	87.7%	96.9%	0.096**
Mean company turnover (annual)	10.0%	10.1%	0.972
Level of tax payment			
central	41.5%	20.0%	0.005*
provincial	47.7%	50.8%	
district	10.8%	29.2%	
Characteristics of company head			
Nationality (head is Laotian)	69.2%	83.1%	0.099**
Mean age (years)	52.6	49.8	0.131
Gender (head is male)	83.1%	75.4%	0.387
Education of head (attended university/college or higher)	83.1%	55.4%	0.001*

*significant at the 5% level **significant at the 10% level. A p-value is a statistical term that measures the likelihood that a difference observed in the sample is due to chance. A result that is significant at the 5% level has a p-value of less than .05. This also means that there is a 95% chance that the value is not due to chance.

Appendix 2. Scenarios for Increasing Coverage

The scenarios depicted in Figure 6 were constructed using data from the Lao Economic Census, and assumptions about the feasibility of reaching each target group. The scenarios are based on assumptions about future compliance, and neither account for population growth nor expansion of the target groups. Nor do they account for the impact of increased compliance on evasion or employment. Validation of scenarios will require more precise data as well as consensus building with key decision-makers about the target group and expected compliance. Although the scenarios are simplistic approximations, they highlight the opportunities and challenges associated with expansion of the target group.

Beginning with the baseline scenario (scenario 1), we see that current compliance stands at 29% of firms but covers 61% of employees. The higher coverage among the latter is a result of covering mainly large enterprises. Given that the infrastructure required to strengthen enforcement is almost non-existent in Laos, considerable effort will be required to increase compliance. Nevertheless, scenario 2 assumes compliance within the current target group reaches 80%. Given the small size of the SSO target group relative to the universe of firms in the country, as shown earlier in Figure 1, increasing compliance to 80% will not result in substantial increases in coverage from a population perspective.

The remaining scenarios illustrate various options for gradually expanding the target group. Scenarios 3 through 7 represent target groups that include all accessible areas throughout the country. In scenario 3, the SSO would continue to target firms with 10 or more employees, and only firms with a tax identification number. Given that most of the firms in areas that are not currently covered are small and medium-sized firms, compliance of scenario 3 is expected to decrease, relative to the compliance level in scenario 2. or illustrative purposes, we assume compliance will decrease to 70%. Scenario 4 targets firms with at least 10 employees who pay any kind of tax. Relative to scenario 3, this scenario adds an additional 83,000 beneficiaries and although compliance is expected to be reduced (to 65%), it may be more cost-effective to target firms that pay any tax, than to only target firms with tax identification numbers. However, identifying these firms may be difficult if the firms have not carried out formal licensing requirements.

The next 3 scenarios represent expansion to groups that are increasingly more difficult to reach. Scenario 5 includes firms with one or more employee with a tax identification number, and compliance is expected to be the same as in scenario 4 (65%). In Scenario 6, firms of any size and paying any kind of tax would be targeted. We assume compliance would fall to 60%, given the difficulty of reaching these smaller, informal firms. Finally, Scenario 7 includes firms of all sizes, regardless of their tax payment. We assume that compliance decreases to 55% for this group. As each new "hard to-reach" group is added, compliance is expected to decrease. Thus, the cost of enforcing enrollment among harder-to-reach groups, such as smaller enterprises and enterprises with less formal tax arrangements, will likely result in diminishing returns in that the premiums collected from these additional groups will be less than the cost of identifying these firms and enforcing enrolment.

Figure 6. *Scenarios for expanding coverage of social security*