Vietnam: Developing a modern pension system – Current challenges and options for future reform

June 2012

Abstract

With declining fertility and rising life expectancy, the Vietnamese population is expected to age rapidly, making the development of a modern social security system a pressing priority for Vietnam. The current system faces a number of major challenges, including low coverage rates in both the formal and informal sectors, inequities between different participant groups, lack of financial sustainability, and weak capacity for management and implementation of social insurance programs. Reforms are needed urgently to expand coverage, promote fairness, improve financial sustainability, and modernize the social security administration in order to help ensure income security for Vietnam’s aging population in the coming decades. This note aims to contribute to the policy discussions around possible revisions to the Social Insurance Code foreseen for 2013 by reviewing some of these challenges and possible reform options.

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1 The note was drafted by Nguyen Nguyet Nga, drawing on extensive background research notes prepared by Paulette Castel. Minna Hahn Tong edited the report note.
List of Acronyms

CPI  Consumer price index
GSO  General Statistics Office
ICT  Information and communication technology
IT   Information technology
MOF  Ministry of Finance
MOLISA  Ministry of Labor Invalids and Social Affairs
NDC  Notional defined contribution
SAA  Strategic asset allocation
SME  Small- and medium-size enterprise
SOCB  State-owned commercial bank
UN   United Nations
VASS Vietnam Academy of Social Sciences
VSS  Vietnam Social Security
I
Introduction

Social security in Vietnam includes social insurance, health insurance, and unemployment insurance, social assistance, and employment programs. Social insurance includes old-age pension and short term benefits (including maternity and protection for income shocks in case of maternity, sick-leave, unemployment, work-injury, old-age, disability and survivorship). With the issuance of the 2012 Party Resolution on Social Security, Vietnam is embarking on a new transition toward a modern social security system.

Vietnam’s rapid economic growth, coupled with major demographic transitions, has given rise to new challenges. Vietnam has achieved remarkable economic growth in the last two decades, transforming itself from a poor agrarian society to a vibrant and competitive player in the global economy. Progress toward reaching middle-income country status, however, has brought new challenges, including the need to reevaluate Vietnam’s pension schemes to meet the rapidly changing needs of its population. Vietnam is expected to undergo major transitions in the coming decades, namely: (i) the social transition from extended, multi-generational families to nuclear ones; (ii) the economic transition from a rural to a more urbanized economy; and (iii) the demographic transition from a young population to an older one.

Figure 1 Vietnam’s population is expected to age rapidly

Vietnam Population Dynamics 1970-2050

Source: World Population Prospects 2010, medium variant

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And family planning interventions.
A particularly daunting prospect is that Vietnam will grow old before it will become rich. With declining fertility and rising life expectancy, the Vietnamese population is expected to age rapidly. Figure 1 presents the United Nations (UN) population projections for Vietnam. The country faces a dramatic challenge: its population aging is still ahead, with the share of its population aged 60 and above expected to rise from less than 10 percent today to close to 35 percent in 2050. Meanwhile, the share of its young population is expected to shrink. There is a need to design a system that is financially sound and with a long-term funding strategy and with institutional arrangements for good governance.

In light of these trends, developing a modern social insurance system is a pressing priority for Vietnam. Vietnam has had a mandatory contributory social insurance system for formal sector workers since 1995. The Social Insurance Law adopted in 2006 introduced significant changes regarding the calculation of pension rights acquired in the private sector, the adjustment of pensions, and the level of contribution rates. The law also determined regulations for the introduction of a voluntary pension system and an unemployment insurance scheme. Despite this progress, however, coverage of the population remains limited, and concerns have been raised over the financial sustainability of the system and fairness. Social insurance delivery also needs to be modernized. In order to deal with these challenges, policy makers will need evidence-based inputs and policy debates that require strong information and financial management system. A well-functioning VSS modern information and financial system management is important not only for proper governance but also for the reform process itself.

This report discusses some of the major challenges in pension policy in Vietnam and presents policy options for addressing them. The report begins with an overview of the current pension system, describing its key features. It then highlights some of the key challenges and proposes measures that could be taken to strengthen and improve pension going forward. The report draws from background notes and analyses that were conducted for this work as well as other recent studies on Vietnam’s pension system. It also identifies potential policy options/decisions that will need to be further elaborated in the next few years.
II
Overview of the Current Pension System

Vietnam’s pension system is defined benefit and operates on a pay-as-you-go basis. Currently, the system is funded by a total social insurance contribution rate of 24 percent, of which 17 percentage points are paid by employers and 7 percentage points paid by employees. Of the total levy, 3 points are allocated for short-term benefits and 1 point is allocated for work injuries and occupational diseases, leaving 20 points for old age, disability, and survivor pensions. In addition to the current 24 percent contribution rate for social insurance, a 3 percent contribution rate is levied for unemployment insurance (split equally among employers, employees, and the Government, using general revenues), and a 4.5 percent contribution rate is levied for health insurance (of which 3 percentage points are paid by employers and 1.5 percentage points paid by employees).

For the pension system, in particular, the 2006 law brought important changes to contribution rates and the adjustment of pensions. The law increased the contribution rates for pensions, setting increases of 2 percent (+1 percent on employer and employee rates) every two years from 2010 until 2014, from 18 percent to 22 percent (14 percent employers and 8 percent employees). Pension adjustments are applied to the total amount of the pensions, and the law foresees that the government decides on adjustment based on general economic trends and inflation. However, since the law passed, the government has continued the previous policy of increasing pensions at the same pace as the minimum wage. Notably, a minimum pension equal to the minimum wage is guaranteed to employees that retire from the mandatory system.

A set of different rules determines the pension rights acquired from work in the public and private sectors. A vesting period of 20 years is required for a person to be entitled to receive a monthly pension equal to 55 percent of his/her average wage. Any contributory year above 15 gives an additional replacement rate of 2 percent for males and 3 percent for females, with the total replacement rate not to exceed 75 percent. For years worked in the public sector, the average wage is calculated on the wages reported in the last ten years. For years worked in the private sector, the average wage is calculated as the average of all the reported wages. Another distinction is that in the calculation of the average wage for pension,

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3 In 2012, the total levy was raised from 22 percent to 24 percent (with the increase split equally between employers and employees). The total levy will be raised again in 2014 from 24 percent to 26 percent (also with the increase split equally between employers and employees).

4 When reaching pension age, retirees with less than 20 years of contributions are entitled to a lump sum amount that is equivalent to 1.5 months of the retiree’s average reported wages per year of contribution. Retirees with 20 years or more are entitled to a monthly pension, plus eventually a lump sum for contributions beyond 30 years in the case of men and 25 years in the case of women.
private sector’s wages are adjusted according to the growth of the consumer price index since the year they were reported while public sector’s wages are adjusted according to the growth of the minimum wage.

The voluntary pension system, implemented in 2008, has a design fairly similar to that of the mandatory pension system for private sector employees. The voluntary system is a defined benefit, pay-as-you-go system. However, unlike the mandatory system, the voluntary system has no short-term benefits, no guaranteed minimum pension, and no possibility of early retirement.

The standard retirement ages are 55 for women and 60 for men. However, private employees and participants of the voluntary system can postpone retirement for five years (until age 60 for women and 65 for men). In the compulsory system, early retirement of up to five to ten years is possible under certain conditions—for example, working in harmful or hazardous occupations for at least 15 years, working in remote areas for at least 15 years, being a redundant employee in the restructuring of state-owned enterprises, or being disabled. The pension formula for early retirement is the same as for standard retirement, except in the case of disability for which the replacement rate is reduced by 1 percent per year of early retirement.

Notably, pensions for individuals who retired before 1995 are paid by the state budget, resulting in two overlapping systems. Until July 1995, when the current pay-as-you-go contributory system was put in place, the Ministry of Labor, Invalids, and Social Affairs (MOLISA) paid pensions to public servants, the military, and members of the Party’s organization. The latter were integrated into the new system, but the government recognized that pension rights acquired before 1995 should remain funded by the State so the costs would not be imposed on current contributors. The current situation is therefore the result of the functioning of two overlapping and entangled systems. The State budget finances about half of the financial burden of today’s pension expenditures. Vietnam Social Security (VSS) and the Ministry of Finance (MOF) are working on calculating budget transfers from the government to cover the costs of current retiring employees’ pension benefits based on the period worked before 1995. The system’s reserves amount to US$5.78 billion, equivalent to 5% of GDP or 7 years of current pension expenditure, given that today about a half of the pension spending are related to rights acquired before 1995.

From May 2012, under the guidance of the newly issued Communist Party Resolution on Social Security, Vietnam is undertaking a new wave of reform initiatives. In the area of pensions, the new initiatives aim at improving the long-term financial viability of the system, reducing the gap between private and public benefits, and increasing coverage. With the target of raising social insurance coverage from 19% to 50% by 2020, it implies that social pensions may not be the only solution to closing the coverage gap, and government will have to find way to increase coverage through supporting voluntary participation. Moreover, improving administrative capacity of Vietnam Social Security agency (VSS) seems to be an un-avoidable path in order to pave way for the policy reforms to take effect.

5 The two systems are entangled because the Social Insurance Law applies to all the participants in VSS. The formula and the adjustment rules do not differentiate between the rights acquired before and after 1995. Consequently, the levels of current pensions benefits—including those obtained before 1995 (for pension adjustment)—are also related to the regulations that rule the current system.
III
Key Challenges

A. Financial sustainability

At first glance, the large reserves accumulated by VSS make it appear that the system is financially sound. In 2010, VSS had accumulated US$5.78 billion of reserves, equivalent to about 5 percent of GDP. The sizeable reserves are a result of the number of beneficiaries being quite small relative to the number of contributors. This is because (i) the scheme was only established in 1995, (ii) much of Vietnam’s labor force is still very young, and (iii) the requirement of 20 years of service for old age pension reduces the number of potential beneficiaries among current elderly. The VSS receives transfers from the general budget to support the payment of benefits to public sector employees who retired prior to 1995.

However, despite these sizeable reserves, Vietnam’s pension system is not financially sustainable in the long term. On an actuarial basis, the VSS is already insolvent because the present value of its projected revenues is less than the present value of its projected expenditures. This is largely attributable to: (i) rapidly declining fertility and the projected aging of Vietnam’s population, which will hugely increase the system dependency ratio—defined as the number of beneficiaries per contributor—from its current value of 0.11 (excluding pre-1995 pensioners) to around 0.50 by 2050; (ii) low retirement ages (average 54.3 years old) relative to life expectancy; and (iii) comparatively high levels of income replacement that reflect high rates of benefit accrual for each year of contributory service, particularly for women employees. In addition, VSS fund returns have been below inflation in greater detail below.
The system is projected to move into deficit in the near future, and the date at which reserves will be exhausted depends on the return VSS will obtain on its assets. Long-term simulations (ILSSA, 2009) show that around 2030, the system will start producing deficits and will stop accumulating reserves. (Figure 2 presents the expected trend of the reserves as expressed in % of GDP). The projections are based on numerous hypotheses, so the forecasted date at which VSS will start producing deficits is not precise. Nonetheless, the projections do indicate the system’s long-term trends. The figure below presents the expected trend of pension expenditures and revenues.

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Figure 2 Vietnam’s pension fund is not financially sustainable in long term

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The projections include many hypotheses regarding formal employment trends, number of pensioners, level of pension benefits, retirement ages, life expectancies, and so on. The main assumptions are: the formal sector is expanding and will represent 50 percent of the working-age population in 2050, the share of private sector employees who reach retirement age and are eligible for pensions will increase from 20 percent in 2015 to 80 percent in 2027, GDP and wage growth rates are 12 percent per year, and inflation is at 5%. However, the future levels of all these variables are unknown. Therefore, the projections cannot precisely predict the size of the VSS pension fund surplus/deficit at a certain date.
Low average retirement age

**Vietnam’s workers retire early given their life expectancy.** As Vietnamese are living longer, the time they will be entitled to pensions is relatively longer than in other Asian countries. Although the retirement age of 55 for women and 60 for men which is already low compared to many other countries, early retirement is so common among public sector retirees that, on average, women retire at the age of 51 and men at the age of 54 (Figure 3). Consequently, pensions are paid over long periods, putting strain on the system. As shown in the right half of Figure 3, Vietnam ranks after China in terms of the gap between life expectancy and retirement age. The gap for Vietnam is even larger if actual average retirement age is taken into consideration.

**Figure 3 Vietnamese workers retire early, and there is a relatively large gap between life expectancy and retirement age**

Growing pension expenditures

In a country where labor’s earnings are growing fast, indexing pension income by the growth rate of the minimum wage (as public wages) has put a significant pressure on the system’s expenditure and future liabilities. This trend is even clearer given the recent effort to unify minimum wages between domestic and foreign direct investment sectors, as required by WTO Accession. However, the pessimistic scenario and outcome illustrated in Figure 4 above could be postponed if some policy changes were introduced. An example of these policy changes are pension indexation at a lower rate than wage growth (e.g. based on consumer price index as illustrated in Figure 4 below).

**Figure 4 Vietnam’s pension fund position if pension is adjusted based on CPI**

![Graph showing pension fund position adjusted based on CPI](image)

Source: Staff estimate based on data from ILSSA, 2009

High pension levels in relation to contributors’ wages

Vietnam’s maximum replacement rate of 75 percent, as the system provides to the public sector’s retirees, is unaffordable by international standards. Men retiring with 30 years of service and women retiring with 25 years of service receive a benefit equal to 75 percent of the wages used in the computation of their benefits. Because in the calculation historical public sector wages are expressed relative to the minimum wage, the resulting pension benefit is rather close to the last wage earned before retirement. As the blue continuous line in Figure 4 indicates, those employees who participate for more than 20 years get, on an actuarial basis, generous pension benefits. An important implication is that unless returns of pension fund investments are higher than regular savings interest rates, the current pension system is financially imbalanced. However, the returns of pension fund investments are not and will not be high enough (or otherwise they will be excessively risky because expected returns are positively correlated with high risks) to finance such level of benefits.
Similarly, the provision that the minimum pension should equal the minimum wage contributes to the financial sustainability problem. People who make contributions based on the minimum wage are entitled to a pension equal to the minimum wage that is higher than the level they can expect if their pension benefit was determined by the pension formula. For example, based on the pension formula a participant who pays a contribution based on the minimum wage for 20 years should, when reaching retirement age, be entitled to a pension equal to 55 percent (or 60 percent for women) of the minimum wage. The law, however, guarantees a minimum pension of 100 percent of the minimum wage. The practice of under-reporting wages will likely result in excessive number of beneficiaries of the minimum pension and contribute in the future to the financial sustainability problem.

### Lack of VSS investment and long-term funding strategy

**VSS current low investment returns reflect an excessively risk-averse investment strategy.** As discussed above, Vietnam has accumulated a significant pension reserve fund, totaling approximately US$5.78 billion in 2010. Until now, VSS fund management has not been diversified and its portfolio is composed only of fixed-income assets. This investment strategy bears little risks but it has resulted in historical low rates of return, sometime below inflation as shown in Figure 5.

![Figure 5: Investment returns of the VSS have remained low.](image)

*Source: Staff estimation based on VSS’s data.*

Furthermore, fund investment capacity at VSS remains limited. The fund likely will not be able to meet future obligations/liabilities if VSS’s investment objectives are not clearly set and if an investment process is not followed. Although the 2006 Social Insurance Law has given VSS management more authority and flexibility in developing investment policy and expanding the investment portfolio, the VSS needs a clearer vision of directions for change and stronger investment management capacity to improve fund management performance.
There is a lack of clarity on who is the real owner of the fund’s assets, as reflected in reporting responsibility. VSS is subject to the overall supervision of a governing board whose chairperson is the Minister of Finance. This architecture recognizes that the State ultimately is the guarantor of pension rights. This institutional setting, however, does not solve the conflict of interest that exists between VSS and the government. As a manager of participant’s contributions, VSS should seek to implement investment strategies that provide the highest returns. Government’ interest, at the opposite, is to obtain funds at the lowest cost. From that perspective, contributions surplus are taxes that give fiscal space and may sustain growth. Contributors in Vietnam implicitly assume that they have a government guarantee for their future pensions, so they have no need to be concerned and be informed about VSS’s performance. Ambiguity over who are the real owners of the fund and how future liabilities will be funded are perhaps reasons why the VSS only has responsibility to report to its board and some government agencies (including MOF, MOLISA annually, and to the National Assembly and Government Inspectorate on a requested basis) but not to its members who make contributions to the Fund (Figure 6).

**B. Fairness**

Inequities are evident across participant groups and Vietnam’s pension benefits are far from actuarial benchmarks. In an actuarially fair pension system, participants’ pension benefits are strictly related to the timing and the amount of contributions, and the average life expectancy of the insured population at retirement age. These principles are applied

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5. Comparing pension systems to actuarially fair saving systems helps understand which individuals are particularly privileged in those systems. The actuarial system usually used for such comparison is a hypothetical system in which the present value of the sum of the contributions plus interests must balance the present value of the sum of the retiree’s expected future pension receipts.
regardless of gender and/or sector (public or private) in which the participants work. In Vietnam, however, pension benefits differ according to gender and sector in several ways, as discussed below.

**Public sector employees are in a better position in terms of pension benefits than their counterparts in private sector.** As mentioned above, different rules are applied in calculating pensions, with the average of the last ten years of wages being used for public sector workers, versus the average of lifetime wages in the case of the private sector. For private sector employees, historical wages are valorized using changes in the consumer price index. For public sector employees, historical wages are expressed relative to the minimum wage for the purpose of computing benefits at the point of eligibility. As shown in Figure 7, the system’s benefits are highly uneven between the public and private sectors, deviating significantly from the market benchmark” or actuarial high case.

![Figure 7. Compared to the actuarial benchmark, the system's benefits are substantially unfair](image)

*Source: World Bank, VDR 2007. Note: Compared between Women (Left panel) and Men (Right Panel), y_axes are replacement rate in % of last wage.*

**Gender differences can also be seen, with female employees being in a better position than their male counterparts.** As discussed above, for any contributory year above 15, women get an additional replacement rate of 3 percent, compared to 2 percent for men. Furthermore, women are entitled to pensions five years earlier than men. Since women’s average life expectancy is higher than men’s, they benefit from the pension system on average for a longer period than men.

**Current levels and the eligibility criteria for disability pensions provide little protection.** Eligibility for disability pensions is very limited and benefits are lower than those obtained by participants that have access to early retirement. Only women aged 45 and older and
men 50 years and older with 20 years\(^8\) of contribution are entitled to disability pension if they have lost 61% or more of their working capacity. Pension benefits are calculated like other pension benefits but the level of the pension in percentage of retiree’s average wage is reduced by 1% for each year of retirement prior standard retirement age. People with disability are much more vulnerable to poverty, and likely require more assistance and health care than other people. Lowering pension benefits and restricting disability pensions to older people is contrary to the mission stated by the government for social security of protecting workers from income shocks and falling into poverty.

C. Coverage

**Basic coverage statistics**

![Figure 8: Vietnam’s coverage is limited (most recent year)](source)

**Source:** TBC

Despite the rapid expansion of pension over the past two decades, only a small share of the working-age population is covered. The analysis of the data of the Enterprise Census indicates that in 2005 that formal employment represented about 6.2 million people (public administration and military excluded); 3.7 million (60%) were covered, 1.2 million (19%) were working under short-term contract and were not covered, and 1.3 million (21%) were working in enterprises that evade social contributions. With a continuing development of the private sector since the 2000’s, coverage has steadily progressed. In 2010, about 9.4 million persons were registered in VSS (including public administration and military). This accounts

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\(^8\) 15 years if the person has worked in specially hard working or dangerous conditions.
for only 21.8 percent of the working-age population, with coverage limited mainly to those in the formal economic sector given Vietnam current workforce of 43 millions of workers. As shown in Figure 8 above, this level of coverage is not low relative to Vietnam’s level of per capita income, but relatively low compared to other countries in East Asia and low perhaps given its aging challenge. This also highlights the significant challenge that government is going to face to achieve its target to expand pension to 50% of their workforce by 2020.

Evidence from 2010 VHLSS suggests that around 10% of the elderly (60++) population receives a pension. Poverty among the elderly was 18 percent in 2010 which is lower than average for Vietnam (20.75 % based on expenditure poverty line of GSO-WB), but given economic, social and demographic changes (including migrations, increasing number of small families, increasing health costs etc.) the living conditions of the elderly risk becoming a serious concern for the Vietnamese society in coming years.

**Participation**

Low coverage of the mandatory system is due in part to a combination of avoidance, policy design, and lack of awareness, and preference for income in the short-term. This low coverage is not only attributable to widespread avoidance, as is the case in many low- to medium-income countries, but also to the rules of the scheme. Farmers and the self-employed— for whom participation is not mandated—still constitute a large share of the workforce in Vietnam. In 2008, Vietnam had 11.3 million non-wage earners, who comprised one-fifth of the working population. In addition, businesses with less than ten employees are under no legal obligation to register with the tax authorities and may erroneously assume that they are also exempted from registering their employees with VSS.

Widespread use of short-term labor contracts also limits coverage of the mandatory system. Analysis of the General Statistics Office’s (GSO) household survey and enterprise census data indicates that in 2006, about 30 percent of enterprise staff or 3 million individuals were employed under short-term contracts or through intermediaries, which are exempted from the obligation to register with VSS (VASS CAF, 2009). It is not clear if the extensive use of short-term contracts stems from enterprises’ need for flexibility or from a desire to avoid paying social contributions. Similarly, 7.7 million employees were working in small business units, many of which do not use labor contracts.

Under-reporting wages, made possible because of regulations loophole, is another factor that allows enterprise evade contribution and pay higher net wages. The reported wage in the labor contract may be much lower than the actual wage paid, in order to minimize the employer contribution for social insurance. Moreover, the reported wage in the initial labor contract is often not changed over time, despite increases in the actual wage. According to a study by the Vietnam Academy of Social Sciences (VASS), this practice is quite popular among

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9 Non-wage earners include three groups: the self-employed and owners occupied in non-agricultural businesses; farmers and individuals working in forestry or aquaculture businesses; and workers who have several types of businesses in and out of agriculture.

small and medium-size enterprise (SME) employers, who may provide higher current salary payment to employees so they can attract more laborers. The study found that contributions were paid on wages that on average represented less than half (42.7 percent) of actual wages. Moreover, less than 10 percent of the enterprises paid contributions on employees’ current wages (VASS, 2009). In exchange for higher current wages, employees may not be interested in enforcing employer SI contributions based on actual wage. The result is a low effective income replacement rate when the workers reach retirement and are entitled to pensions.

Coverage of the voluntary system remains very low, mainly because its design is not attractive to new participants. Take-up rates in the voluntary scheme were rather low in 2009 and 2010, with participation being largely dominated by individuals who moved out of formal wage employment and wanted to complete the required minimum contributory period for pension rights before reaching retirement age. The institutional design of the scheme may be discouraging participation: participants need to have contributed for at least 20 years to be entitled to a pension, otherwise an old-age lump sum benefit will be paid. As mentioned above, the lump sum for a short contributory period is equivalent to 1.5 months of the retiree’s average. Women in their early 40s and men in their mid-40s therefore have little incentive to enroll. Take-up rates for younger workers are also low, perhaps partly due to lack of public awareness of the program and possibly also to the absence of a minimum pension guarantee, which may contribute to a general perception that its provisions are less attractive than those of the mandatory scheme.

Vietnam’s pension benefits are considered generous for public sector employees as compared to those earned in the private sector. Several reasons explain this. Firstly, the definition of the average wage on which pensions are calculated creates an important gap between the two sectors. As mentioned above, while public sector wages are adjusted according to the growth of the minimum wage, the reference is the CPI for the wages of the private sector. It is important to observe, however, that on an actuarial basis, the benefits paid to the public sector’s retirees are largely above the levels these participants could expect from similar amount of scheduled savings in the financial sector. Secondly, pensions are proportional to the number of year of services. Employment in the private sector is not as stable as in the public sector and private sector’s employees reach retirement age with likely less number of years of service than their colleagues of the public sector. On an actuarial basis, the benefits paid to the persons that reach retirement with less than 20 years of service are particularly low. Thirdly, the practice of under-reporting wages is widespread in the private sector. It implies that pension benefits replace a rather small share of employee’s income.
Most likely outcomes without reforms

Since a large proportion of the labor force is in the informal sector, it is likely that less than half of the elderly will be entitled to pensions around 2050. As shown in Figure 9, only a very small number of elderly are projected to retire under the voluntary system. If the incentives for participation in the voluntary system remain low, less than half of the elderly population is projected to be entitled to any type of pension by 2050. Women in their early 40s and men in their mid-40s therefore have little incentive to enroll.

Hình 9. Người nghỉ hưu và người già không có lương hưu

Nguời hưởng lương hưu và người cao tuổi không có lương hưu

Notably, a significant proportion of workers are low-income earners who likely cannot afford participation in the pension system. Low-income earners include all individuals who earn individual income lower than the minimum wage (in a year). According to the 2008 GSO household survey, Vietnam had 13.1 million low-income earners in 2008. Although all of these persons are not necessarily poor, the poverty incidence among this group is particularly high: as shown in Table 1, 38.2 percent of these individuals were poor or near poor in 2008. These individuals more likely cannot afford to participate in the social security system, which has implications for coverage of the system as well as for poverty among the elderly.

Table 1  Employment and poverty status of the working-age and elderly population

<table>
<thead>
<tr>
<th></th>
<th>Non-poor</th>
<th>Non-poor Poor and near poor</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Wage earners</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Individuals registered in VSS</td>
<td>94.0</td>
<td>6.0</td>
<td>100</td>
</tr>
<tr>
<td>Individuals under short-term contract or in enterprises avoiding registration in VSS</td>
<td>91.6</td>
<td>8.4</td>
<td>100</td>
</tr>
<tr>
<td>Individuals in very small business units not registered inVSS</td>
<td>83.4</td>
<td>16.6</td>
<td>100</td>
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<tr>
<td><strong>Non-wage earners</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Self-employed in non-agriculture sectors, owners</td>
<td>95.2</td>
<td>4.8</td>
<td>100</td>
</tr>
<tr>
<td>Farmers</td>
<td>82.6</td>
<td>17.4</td>
<td>100</td>
</tr>
<tr>
<td>Individuals in farming and non-agriculture sector</td>
<td>86.5</td>
<td>13.5</td>
<td>100</td>
</tr>
<tr>
<td><strong>Low income earners</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pensioners and inactive</td>
<td>87.9</td>
<td>12.1</td>
<td>100</td>
</tr>
<tr>
<td>Early pensioners</td>
<td>92.8</td>
<td>7.2</td>
<td>100</td>
</tr>
<tr>
<td>Individuals with no working activities</td>
<td>87.8</td>
<td>12.2</td>
<td>100</td>
</tr>
<tr>
<td><strong>Total working age population</strong></td>
<td>82.2</td>
<td>17.8</td>
<td>100</td>
</tr>
</tbody>
</table>

11 Near poor is defined as being in a household with consumption per capita is 130% of those in the first quintile.

Note: * defined as living in a household with consumption per capita is 130% of those in the first quintile.

Source: Castel policy note 6, 2011.
A significant share of the population may not be eligible for a pension. The classification of the working population below retirement age in 2008 by professional and social insurance status helps to distinguish 3 particular groups: (i) those participants who have less than 20 years of pension contribution and who will get a lump sum benefit (15%), (ii) those who have less than 20 years of pension contribution, will get a lump sum benefit at retirement age, and are poor (11.6%), and (iii) those participants who would be eligible for lump sum benefit at retirement if they continue to contribute to social insurance (0.8%).

**Hình 10. Phạm vi trợ cấp hưu trí tại tuổi nghỉ hưu**

- Đều hưởng lương hưu khi nghỉ hưu: phân chia (theo %) của dân số lao động

![Pie Chart](chart.png)

- 57.3% Covered and eligible for pension at retirement
- 15.0% Not covered, only eligible to lump sum benefit at retirement if contribute - Not poor
- 11.6% Not covered, only eligible to lump sum benefit at retirement if contribute - Not poor
- 15.4% Covered only eligible to lump sum benefit at retirement
- 0.8% Not covered only eligible for pension at retirement if contribute

Source: Paulette (2011)

**D. Implementation and management**

Despite the considerable reform efforts underway, the social security administration continues to face several major challenges. These challenges include low compliance by the non-governmental formal sector, low coverage of the poor and targeted groups, and vulnerability in financial sustainability. Furthermore, although the Government’s commitment to reforming the social security administration is very strong, the institutional capacity of VSS to implement such a complex undertaking remains a concern. And in addition to social and unemployment insurance, VSS is also in charge of administrating the health insurance scheme.

Vietnam’s social security administration has not kept pace with the rapidly changing needs of a formalizing and industrializing economy and an aging population. VSS runs a largely decentralized, uncoordinated and partially manually-based system with low compliance and coverage. Its business processes require a strategic review and re-engineering so as to streamline its operation and makes it more effective in meeting expanding needs. Challenges include a decentralized processing system, with most business functions being handled at the provincial and district levels without a connection to the central level and...
without a centralized database; VSS’s calculation and re-calculation of contributions due from employers, which impose a heavy administrative burden on the VSS; lack of integration with the Tax Administration, which lead to under-collection of contributions; a lack of integrated database and information systems for monitoring and evaluation in particular of the profile of the contributors and pension outcomes and the significant administrative challenges posed by the Health Insurance Law’s implementation, which will result in significant increase in number of participants in HI scheme.

Another issue to be addressed is the assignment of personal identification numbers. All persons registered in the state social insurance system should have a unique Social Security Number for identification purposes. It should remain with them throughout their participation in social insurance, irrespective of the district or province in which they reside. Currently, the VSS provincial-level offices assign identification numbers locally, without coordination or crosschecking at the national level to ensure each number is unique. The absence of unique individual numbers may lead to system mistakes and complex electronic data processing in the area of social security. Assignment of individual numbers is even more complicated in the health insurance system, with individuals being required to re-register and obtain new numbers each time they move to a new location.

VSS also has weak IT planning and support capabilities. A comprehensive IT plan is needed to develop common information environments for such standard tasks as contribution collection, calculation of benefits, benefits payments, budget planning, and budget accounting. However, no overall framework or plan has been developed to guide the development and deployment of IT within the social security system. Furthermore, the system suffers from lack of a nationwide high-speed telecommunications network and connectivity between the central, provincial, and district offices, which hinders information flow and constrains the proper gathering and verification of necessary information. The payment process is cumbersome and requires excess paper flow. No uniform concrete solutions have been developed for individuals’ identification, hardware platform, system software platform, data replication, data security, and so on. The central VSS IT department is searching for IT solutions, but in the meantime, some provinces have IT departments and are developing their own software applications, which can weaken data integrity and security.
IV
Options for further reform

The above analysis points to key areas where further reforms are needed to develop a modern pension system for Vietnam. Greater efforts are needed to expand coverage of the compulsory system and of the self-employed/informal sector, improve fairness, ensure financial sustainability, and strengthen implementation and management. Potential reforms in each of these areas are discussed below.

A. Ensuring financial sustainability

Reforming pension policies

To improve financial sustainability, contributions and pension rights should be based on actually paid wages. Convincing enterprises and employees to pay contributions on the totality of wages will help increase VSS resources. It should be noted that while these changes will postpone the date the systems runs deficits, they do not solve the problem of long-term deficits since the pension formula is too generous given Vietnam’s current demographic trends, employment, and retirement behaviors. Close cooperation with Tax inspectorate could help in this matter, since it is beneficial for enterprises to report total labor cost to the Tax inspectorate in order to reduce incorporate taxes.

Workers preference for higher net wages and enterprises’ difficulties to retain workers suggest that moving out of the existing status quo requires an overall strategy. The enforcement of making contribution payments based on total wages may not be likely without complementary measures. It requires that workers are willing to forego part of their current salary for future pension benefits. For that purpose the reform must include a set of interventions that change the perception of private sector workers that “social contributions are like taxes rather than savings”. These interventions may include measures that increase the eligibility and the level of pension benefit to the persons that will retire in the coming decade from the private sector. These measures should not modify the pension formula because in the medium-term, if contributions are paid on actual wages, pension benefits will improve. It requires also changing workers’ attitude towards social security through information campaigns but also reforms that make the system more equitable and VSS operation more efficient.

Expanding coverage is a strong driver of financial long-term sustainability. Although not directly profitable, investing resources in supporting participation and expanding coverage among workers will widen VSS’s contributory base and bring positive financial returns. Such spending is therefore financially beneficial for the system.
Controlling growth of pension expenditures

Given the system’s expected amount of resources, policy makers must consider the tradeoff between eligibility (mostly retirement age) and level of benefits. Changes in the pension formula and in pension age should be introduced sooner rather than later to enable a more gradual approach. The pension formula could be adjusted using parametric reform (e.g., gradually raising retirement ages, adjusting indexation to the CPI, adjusting the minimum pension level) or NDC accounts, as discussed above. Employees may resist changes in the formula, since their welfare may be affected. Again, the sooner the changes, the easier it will be since few employees have sizeable savings now. If the reform is introduced early enough, the necessary changes can be introduced gradually, and participants and their families will adjust as the new system phases in and the country develops. If reforms wait until the pension system starts running deficits, the number of pensioners and contributors will be much higher, and the system will not have enough resources to smooth the impacts of the reform on beneficiaries and participants. Delaying such reforms will therefore be more difficult and more costly for society.

To reduce financial pressure on the pension fund, other social policies should be financed from different sources. These could include early retirement option and compensation benefits for redundancy workers resulted from SOE reform, early retirement by employees from special professions and/or jobs (such as military, police, mining, and jobs in remote areas). Since these are part of social policies, the cost (lower pension benefits) of these programs should be made explicit and VSS could consider option to request Government funding to implement such social policies. For example, the government would pay the benefits over the early retirement years, while the pension funds would pay the benefits from the standard age of retirement and after.

Strengthening pension fund investment management capacity

To strengthen pension fund investment management capacity, an authorizing environment and governance structure need to be created. This would involve the establishment of an Investment Committee under the overall direction of the Governing Board to strengthen highlevel capacity for handling specialized investment management issues. This could help pave the way for adopting a three-tier governance structure for VSS, under which: the Governing Board would be responsible for high-level decisions, including those related to investment policy, risk tolerance, and staffing; an Investment Committee that reports to and acts within delegated powers from the Board would have principal responsibility for formulation of investment policy, strategic asset allocation, and oversight of investment operations; and investment management staff would be responsible for day-to-day investment operations. The governance of the Governing Board should take into account that, beyond the need to provide strategic guidelines on the investment policy, the latter will probably need to deal with several conflicts of interest. The first one, as mentioned above, is that Government is more likely willing to drain VSS funds at low cost. Second, implementing subsidies such as the policies suggested above could produce lower returns (higher amount of contributions) than pure financial investment strategy. The composition of the Governing Board, the mandate of each member and their monitoring/evaluation/communication strategy should therefore be determined in accordance.
Human resources and training will also be critical for building investment management capacity. The newly created Investment Management Unit should be staffed with a core group of investment management professionals who have specialized investment management expertise.

Adopting a formal strategic asset allocation (SAA) framework could provide VSS with an anchor for its investment decisions. An SAA framework would allow the fund to systematically identify and adopt a preferred asset allocation mix based on the objectives of the fund, the risk tolerance envelope (including an appropriate investment horizon), and practical market-based considerations. In the case of a pension fund such as that managed by VSS, it is not merely asset performance in and of itself that is of consequence, but rather how well the assets do in relation to the liabilities they are expected to fund. For this reason, it is important to have timely and updated information on the projected liabilities before a meaningful SAA can be established.

Even before the adoption of an SAA framework, diversification of the asset allocation mix would be desirable. The current asset allocation mix, with its exclusive reliance on nominal fixed income securities, could leave the fund vulnerable in the event of a sharp and sustained uptick in inflation and/or real wage growth. This would cause the investment portfolio as it is currently structured to underperform the growth rate in liabilities, potentially leaving the fund unable to deliver on benefit payments that have fully kept pace with real wage growth. A strong case can therefore be made for diversifying the asset allocation mix, including making an allocation to equities as part of the SAA. Even before the formal adoption and implementation of an SAA framework, VSS should consider steps for increasing the share of its investments in publicly traded and marketable bonds in relation to investments in privately negotiated loans to the State budget and state-owned commercial banks (SOCBs).

It will be increasingly important for VSS to develop and build risk management capabilities, based on periodic market value assessments of the portfolio. Currently, VSS does not have any risk management infrastructure. Building risk management capabilities is an especially important prerequisite before VSS can begin to consider expanding the range of its investments.

Measures to improve accounting, reporting, and the use of performance measurement and benchmarks would also enable sound investment management. Reporting on investment management and performance to the Governing Board should be enhanced to include details on portfolio composition, maturity profile, and the interest rate structure of the outstanding investment portfolio, as well as performance by investment type both in absolute terms and on a relative-to-benchmark basis. The potential for measuring and reporting on such asset-liability measures at least on an annual basis should also be explored. It is important that the calculation and classification of investment performance are made by investment type, to provide information on the relative efficiency of different types of investments and help ongoing decision-making. The same is recommended for establishment of benchmarks for evaluating the investment performance of each investment type and the aggregate portfolio, as well as for monitoring and evaluating investment management expenses and other costs.
B. Improving equity

Equalizing treatment of public and private sector employees and male and female workers will not only ensure fairness in the pension system but also help improve the system’s longterm sustainability. In terms of sector equity, a gradual approach should be used to convergence pension formulas towards the pension formula used for private sector workers. The sooner the reform, the easier it will be to introduce changes at smaller cost. In terms of gender equity differentials in retirement age and pension formula should be eliminated. International experience shows that a gradual approach is needed—for example, the current retirement age for women could be increased by four months every year until reaching the same general retirement age as men. Similarly, the pension formula for women could be gradually equalized to the pension formula of men.

The option to shift to Notional Defined Contribution (NDC) system should be considered over the longer term, but with caution. The advantage of NDC accounts is that because they mimic savings accounts they make apparent the value of any cross-subsidies. NDC systems record employees’ contributions, not employees’ wages. Rather than computing pension receipts on employees’ average wages and number of years of contribution, NDC systems calculate pension receipts on the capital—contributions plus notional interests—each retiree has saved in the system given the age at which the pension is claimed. The pension formula may appear to be more complex, but because the NDC system strengthens the link between contributions and pension benefits and reduce participants’ inequities, it is more transparent and easier to understand. However, shifting to NDC system also implies substantial changes in benefits that might not be politically expected (more substantial increase in retirement age as compared to gradual increase as currently debated, lower pension, etc). Moreover, NDC systems require considerably stronger administration systems than that currently available to VSS.

C. Expanding coverage

There are several measures that could be considered to expand coverage of the pension scheme. Possible measures include the following:

- Extending compulsory participation to all employees with a labor contract. Ideally, the pension system should cover all wage earners including those on self-employment income. However, in practice there is a problem of enforcement (on whatever legal basis) especially given VSS’s current administration capacity. For that reason, universal mandatory participation is not an easy and feasible solution at this stage (it is already a challenge with expanding health insurance coverage). Eliminating legal loopholes, increasing cooperation with tax authorities, improving VSS enforcement capacities are of major importance for improving coverage. Informal employment in the enterprise and in the informal sector is, however, substantial and, more likely, difficult to tackle without institutional changes.

- Encourage voluntary participation. Therefore in order to realize ambitious target on coverage set in Party Resolution, alternative options that encourage voluntary participation (through providing incentives, and/or partial subsidies) and address future poverty (through providing non-contributory social pensions to the poor elderly without pension income) must be carefully studied. In any case, fiscal and poverty impact analysis should be carried out to assess policy’s feasibility.

- Other complementary measures should be analyzed further such as increasing workers’ awareness about their opportunities to earn a meaningful pension
through participation in their early working life. For relatively older participants who would receive a lump sum at retirement, opportunity for them to obtain pension income when reaching retirement age (through purchasing missing years of contributions) should be considered and fiscal impact analysis should be done to assess policy’s feasibility.

**Subsidizing contributions of the poor, near-poor and low income workers is affordable.**

Table 2 below presents some tentative estimates of the State subsidies the contributions of (1) the poor, the near poor and the low income earners who cannot afford participate in social insurance and, (2) of the youth so that they get acquainted to social insurance and increase their chance to contribute for 20 years during their working life. Considering that the minimum contribution amount to 18% of the minimum wage in 2011, subsidizing one year of contribution represents a cost of VND 1.8 million per individual. In 2012 and 2014, the increase in the contribution rate will increase this cost up to VND 2.0 and 2.2 million, respectively (at 2011 prices). From the Table 2, subsidizing participation would cost 0.07% of GDP for the poor and the near poor and another 0.0.7% of GDP for the low income earners. The cost of subsidizing the participation of the young workers would cost around 0.02% of GDP. The budgetary impact Formatted of this policy over the next 20 years would be rather low. Because VSS is in surplus, all the additional income it collects in contribution could be redirected to the State budget through the government’s sales of public bonds to VSS. Subsidizing contributions would only increase the State’s future debt to VSS and the pension system.

**Table 2 Cost of subsidizing participation (2011 prices)**

<table>
<thead>
<tr>
<th>Number of beneficiaries</th>
<th>Cost per beneficiary</th>
<th>Total cost</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>VND million per year</td>
<td>VND billion per year</td>
</tr>
<tr>
<td>Poor and near poor</td>
<td>8,092,514</td>
<td>1.8</td>
</tr>
<tr>
<td>Low income earners</td>
<td>11,900,000</td>
<td>1.8</td>
</tr>
<tr>
<td>Young participants</td>
<td>1,424,817</td>
<td>1.8</td>
</tr>
</tbody>
</table>

*Source: Castel policy note 6, 2011.*

Rather than relaxing the rules on contributions to encourage participation, it would be more prudent to increase the opportunities for worker to receive pension income. Although requiring 20 years of contribution to obtain a pension is a major impediment to participation, relaxing this requirement does not appear to be the best policy option, at least until mandatory participation for all is enforceable. Rather than reducing the vesting

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12 Retirees who contribute few years should, in principle, be entitled to small pensions. However, delivering small pensions to retirees is socially unsustainable, particularly if the recipients are low-income earners and, consequently, the pension system and the government come under pressure to increase these pensions. The resulting higher benefit increases the incentives to contribute only over short-periods. Participant that could contribute higher amount or over more years to the pension system—obtain a free ride (higher pensions without having paid the corresponding contributions). For this reason, any reforms that lower the requirement of 20 years of contribution is difficult to implement as long as l mandatory participation for all is not enforceable.
period of 20 years, pension entitlement can be made more flexible for a certain transitional period for individuals who are near retirement age today. These people could be given the opportunity to buy the missing years of contribution they need to complete the requirement for pension rights. State or VSS subsidies could help reduce the cost of the process for certain vulnerable groups.

An alternative would be to allow workers the opportunity to buy missing years of contributions. Options to buy missing years and associate costs are presented in Table 3. The simulation from which these figures are taken assumes that the system provides a pension benefit equal to 60% of the minimum wage at retirement and indexed to consumer prices growth during the retirement; that VSS is able to earn 5.4% above the inflation on the funds it collects and the combined average life expectancy of the retirees at age 60 for women and at age 65 for men is of 20 years (see Annex 1). The contributions paid by the retirees during their working life are transformed into valued pension rights with the same approach. The value of the missing years corresponds to the gap between the value of these pension rights and the amount of capital needed to finance pension benefits during old-age. Table 2 gives the resulting cost of the missing years at 2011 prices. The capital VSS requires to provide a pension benefit equal to 60% of the minimum wage at retirement (and indexed to consumer prices growth during the retirement) is estimated to VND 75.8 million or 3 678 dollars in 2011.

<p>| Table 3  Cost of buying additional year |</p>
<table>
<thead>
<tr>
<th>Missing years</th>
<th>VND million</th>
<th>US dollars</th>
<th>Missing years</th>
<th>VND million</th>
<th>US dollars</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 years</td>
<td>6.0</td>
<td>290</td>
<td>11 years</td>
<td>51.2</td>
<td>2485</td>
</tr>
<tr>
<td>2 years</td>
<td>11.6</td>
<td>565</td>
<td>12 years</td>
<td>54.5</td>
<td>2647</td>
</tr>
<tr>
<td>3 years</td>
<td>17.0</td>
<td>826</td>
<td>13 years</td>
<td>57.7</td>
<td>2801</td>
</tr>
<tr>
<td>4 years</td>
<td>22.1</td>
<td>1074</td>
<td>14 years</td>
<td>60.7</td>
<td>2947</td>
</tr>
<tr>
<td>5 years</td>
<td>27.0</td>
<td>1309</td>
<td>15 years</td>
<td>63.6</td>
<td>3085</td>
</tr>
<tr>
<td>6 years</td>
<td>31.5</td>
<td>1531</td>
<td>16 years</td>
<td>66.3</td>
<td>3217</td>
</tr>
<tr>
<td>7 years</td>
<td>35.9</td>
<td>1743</td>
<td>17 years</td>
<td>68.8</td>
<td>3341</td>
</tr>
<tr>
<td>8 years</td>
<td>40.0</td>
<td>1943</td>
<td>18 years</td>
<td>71.3</td>
<td>3460</td>
</tr>
<tr>
<td>9 years</td>
<td>43.9</td>
<td>2133</td>
<td>19 years</td>
<td>73.6</td>
<td>3572</td>
</tr>
<tr>
<td>10 years</td>
<td>47.7</td>
<td>2314</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Castel policy note 6, 2011. Estimations based on VSS and GSO data

Similarly, any expansion of non-contributory social pensions for elderly without pension income should be considered very carefully. Currently, a non-contributory social pension of 180,000 VND per month is provided to elderly over 80 years of age if they have no pension or other social support. Expansion of the policy to all elderly without pension income is under discussion, but there are two reasons to proceed with caution. First, expanding social pensions may discourage participation in contributory pension schemes. Second, estimates show that such a solution would be expensive in the long term. For example, providing a social pension equivalent to 55 percent of the minimum wage (which is equal to the minimum pension provided by the voluntary pension fund) to all elderly 70 years and over in rural areas

13 About 40.3 dollars per month in 2011
14 Decree 13/2010/N-CP.
Ten muc could cost around 1 percent of GDP in 2030. Providing a social pension of 180,000 VND or 25 percent of the minimum wage to all elderly above the standard retirement age in rural areas could cost 0.5 percent of GDP in 2030. Targeting social pensions to the most vulnerable and poor elderly within the social assistance and poverty alleviation programs could help contain costs and increase the efficiency of such programs.

**International experience shows that facilitating voluntary participation (with incentives and/or partial subsidy) has not been not very successful.** Most voluntary schemes around the world have failed to generate much participation among lower wage and informal sector workers, even with fairly generous subsidies. Additional work will be needed to simulate options following both directions (subsidizing contributory participation and non-contributory social pension) to provide evidence-based inputs for policy makers to make informed decision on how they would like to expand pension coverage. This could also inform potential participants on the possible trade-off between having a reasonable pension in the future and a social pension which is design to protect against poverty among the elderly.

**D. Modernizing the VSS administration system and improving implementation**

In light of the major transitions that are expected to take place in Vietnam in the coming decades, the development of a modern social security administration is a pressing priority. Not only is improved social security administration required to collect contributions from a growing number of private enterprises and informal sector employees, a high quality social security administration is also needed to improve the investment environment, boost private sector development, and ensure an effective pension system. The system should foster labor mobility and minimize distortions to work incentives.

As a starting point, VSS needs a clear reform strategy for improving the efficiency, performance, and accountability of the social security administration over the next ten years. The VSS reform strategy needs to lay out a vision of a modern social security administration system for coming decade, while sequencing implementation to develop a system that is in line with international best practices. It should also anticipate the needs for key physical and human capacities to enable the effective development and roll-out of the new modern administration system. In addition, it should attempt to foster better coordination/harmonization between the Tax Administration and VSS management for collection and integration in the longer term.

**Strengthening the operational efficiency and capacity of VSS will require efforts on multiple fronts.** Improving business processes and information management, enhancing service to clients, and increasing transparency are the main areas for attention. An important measure in this regard will be to develop a unified ID number for VSS beneficiaries as well as a solid data management system, including for historical contribution records. This will help VSS in consolidating and cleaning the data on individual earnings and contribution histories and also help ensure consistency and robustness of recordkeeping within the institution across various programs (pensions, unemployment, health insurance).
Fostering better coordination between the involved government institutions will be important for improving the delivery of social security services. The current division of labor—with MOH, MOLISA, and MOF responsible for policy making, while VSS handles implementation—is one of the strengths of the Vietnamese approach to social insurance, such as to avoid possible conflict of interests. In practice, however, some overlaps in functions and weak coordination among these institutions may pose risks to the modernization of the social security administration. Appropriate VSS data should be made available in real time for other agencies to analyze and use to inform policies, which will in turn make the task of implementation less challenging for VSS. Better coordination/harmonization/integration in some key functions such as collection and/or payment could help to improve efficiency as well as allow VSS to focus on strengthening administration of it remaining functions and improving its services.

A related priority is to develop a centralized database for the social security system. To enhance VSS’s data control capacity and maintain efficient functioning of the personal insurance accounts system, all records on insured individuals, pensioners, and employers should be stored and processed on VSS’s central servers. The central database should also contain information such as management rules, control criteria, and reports. A central database system would enable 26 VSS officers to track contribution/employment history and easily calculate and assign pension benefits. The information could be used by the relevant departments of VSS as well as made available to insured individuals through the Internet or local branches to inform them of VSS activities and enable them to see the current balances of their individual accounts. The establishment of a central database system will help improve transparency, simplify management, and facilitate the gathering of necessary information for informed policymaking on social security.

It should be recognized that IT-related improvements and other reforms are interdependent in many respects, making the reform process more complex. IT support and HR development depend on progress in social security policy as well as business process reengineering. At the same time, key social security administration processes can only function properly with effective IT support and sufficient staff capacity. Therefore, the sequence of interrelated IT, business process re-engineering, and HR reforms must be carefully designed and implemented.
V
Conclusions and proposal for further technical support

Conclusions

Vietnam’s social security reforms will require careful balancing and phasing. A “package approach” that links reforms should be pursued, balancing politically difficult parametric adjustments to the compulsory fund with measures to make joining the pension system more attractive. At the same time, such policy reforms will need to be linked with efforts to strengthen the delivery capacity of VSS and the administration system. As discussed above, introducing reforms sooner rather than later will enable the more sensitive reforms to be phased in gradually, with less social impact and less risk of undermining support or discouraging participation.

It should also be noted that some policy reforms that are currently being proposed in Vietnam could have adverse effects. For example, the further increase in the contribution rate that is currently being implemented under SI Law to help deal with cost pressures could eventually harm job creation and may result in increased avoidance of social insurance contribution, or negative impact on wages. In Germany, the government has tried several different measures to avoid the need to increase the contribution rate beyond 20 percent. The reforms that are being proposed in Vietnam should therefore be scrutinized carefully to ensure that they will be beneficial to the social security system and the country’s aging population in the long run.

Vietnam lacks an overarching social protection system framework to provide policy consistency across its different programs, many of which are poorly linked with one another. It is less clear on how to adopt a systematic approach to social protection development. Such an approach emphasizes the importance of:

• Exploitation of interactions between programs to (i) eliminate gaps in coverage (such as those being faced by the working poor in Vietnam), (ii) improve incentives, both by discouraging adverse behaviors and by developing interlinked policies that reinforce desirable behaviors (with particular attention paid to the impact of social protection initiatives on the incentives for the formalization of the labor market in Vietnam).

• Sharing of resources across programs to (i) leverage economies of scale and scope (for example by deploying the same administrative and information technology systems to support multiple programs or administering, monitoring, and evaluating multiple programs with the same personnel or same governance structures) and (ii) reduce distortions in the labor market created by separate financing arrangements.
Next steps: Scope for further analytical work and technical dialogue

This note has identified policy reform areas in which further elaborated technical inputs will be needed before potential policy options/decisions can be adopted and incorporated in the revised social insurance law and subsequent sub-law regulations. Future work could take the form of providing technical inputs and organizing workshops for knowledge raising and consensus building. Particularly, technical inputs may include, but not limited to:

- Analysis of the potential impacts and consequences of alternative reform scenarios (e.g. shifting to NDC system vs. parametric reform; subsidized contributory pension vs. noncontributory social pensions, converging pension formula towards that of private sector workers, fiscal and poverty impacts, etc), identifying the winners and losers in each case, and assessing the corresponding funding strategy;

- Research on key parameters in a way that is conducive to the analysis of pension reforms (life expectancy of current pensioners, working profile of current contributors, number of participants not eligible for pension at retirement, amount of cross-subsidies related to early retirement etc.).

- Exploring opportunities for further technical support to VSS to develop its strategy to modernize social security administration system.
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Developing a modern pension system – Current challenges and options for future reform

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