Social Security Arrangement in Nepal: Needs and Challenges Ahead

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Abstract

This study primarily examines the prevailing social security schemes in Nepal and tries to explore needs and challenges ahead. In Nepal, government initiation for providing social security services was made back in 1930s. Before the installation of multiparty democratic system in 1990, there were only two schemes, namely Employees Provident Fund and Pension covering only government sector employees. Having trifling importance until early 1990s, EPF made significant progress thereafter. It extended coverage to private sector employees and fringed additional schemes that enlarged members' choices and privileges. However, despite the dominant scheme of social security, its coverage is stringently limited and can hardly cover large portion of lower-income people even in near future. Pension scheme operates as a non-contributory plan for employees in government sector and selected institutions. Citizen Investment Trust, a voluntary saving scheme introduced in early 1990s, primarily aims to contribute capital market development by encouraging individuals to mobilize saving in tax-exempted manner. Recently introduced Allowance scheme pays elderly and incapables with small sums of cash benefit. In aggregate, government employees and elderly people are in the center of existing arrangement while integration is lacking among the schemes. Further, notwithstanding the poverty-ridden societies and widening income disparity in Nepal, there is no considerable provision for risk pooling and income redistribution. Similarly, efforts are lacking to bring health services into social security ambit. In effect, existing structure favors those who are relatively in better-off situation. Notably, notwithstanding the noteworthy expansion in recent years, large part of the population remains beyond social security coverage and the system is still in its infancy. Prevailing circumstances of limited coverage, fading out of traditional measures, widening risks and increasing public consciousness on social security have jointly necessitated for the expansion of social security services in the country. Finally, having poor financing capacity of both government and the public, government commitment and the public eagerness to join the system are important for universalizing the coverage in Nepal.

Key Words: Social Security, Social Protection, Social Policy, Provident Fund, Nepal

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1. Introduction

The pace of decentralization is very slow with dominance of centrally planned economic policy in Nepal where substantially high percentage of population lives in rural area remaining beyond the influence of mainstream economy. In addition to the large volume of gross domestic product originating from rural-based subsistence agriculture, informal activities considerably contribute to non-agriculture sector. Schneider (2002) estimates that more than 38 percent of the gross national product in Nepal originates from the informal economy while Nepal Human Development Report (2004; 92) writes, almost 90 percent of the employment remains concentrated in informal sector without adequate provisions for social security benefits. Around 84 percent of total populations, who are rural residents, have very poor access to socio-economic infrastructure, remaining far behind than their urban counterparts in many grounds. Human Development Index for urban and rural area is respectively 0.581 and 0.452 when the overall index was estimated 0.471 for 2001. Life expectancy in mountain trail is lower by eleven years than that of Tarai while the urban-rural gap is four years. Moreover, figures like around only eight percent female participation in civil service, 34 percent adult literacy of female compared to 66 percent of male and 26 percent lower wage (than male) paid to female in non-agriculture sector reflect huge gender gap in Nepalese economy. In overall, because of the top-down development pattern, practice of biased social values and traditional creeds, and lack of minimum protection against social risks[2] and vulnerabilities, poverty has remained widespread, income inequality is widening further and gender disparity remains substantial in Nepal.

However, recently, from the consideration of both economic development and basic needs perspective, social sector has received increased priority in policy level. Ongoing national plan (Five-year Tenth Development Plan, 2002-2007), which is itself country's Poverty Reduction Strategy Paper (PRSP), differs from the past and explicitly identifies social exclusion as one of the fundamental development challenges. Nepal Human

2) Social risk is a dynamic concept-insecurity means exposure to risks of events that if they occur, result in further vulnerability (ADB, Webpage, 2006).

Development Report (2004; 12), by identifying empowerment the most important agenda at present, argues on the need of deeper and faster social, economic and political transformation towards the development of an equitable, non-exclusionary society and a democratic, rights-based polity. Though no statistical support can be presented, high social risks and vulnerability is also one of the prime reasons in the country causing low level of productivity. In such circumstances, a well-designed social security system can be expected to have multi-fold effects for maintaining basic living standard to greater population while minimizing various risks and fostering redistribution of income and opportunities.

Unfortunately, notwithstanding the importance of social dimension recognized in development discussion, there is no single institution in Nepal that is explicitly mandated for supervising social security affairs nor the concept of social security has gained due consideration in policy formulation until very late. In fact, from present 17 percent of social protection coverage[3)], Nepal has a long way ahead to develop the system covering whole population universally. Obviously, many people with no means of protection belong to the economically weaker sections of society (Beattie, 2000; 147). Since the neediest and rural population in developing countries do not generally have access to the existing formal schemes so greater government exercise is necessary to ensure basic social needs to all. Moreover, many developed countries, which are having heavy burden of social security system in the face of ageing, are teaching important lessons that appropriate track should be initiated from the very beginning to make the system sustain long. In these surroundings, present challenges for Nepal is not only expand social security services but also suitably modify/reform the system for its sustainability.

Along with the widening risks and vulnerabilities, countries are designing social security systems with wider coverage depending on their specific needs and capacity. Traditionally developed pay-as-you-go based schemes are said to be unsustainable in the face of changing demographic composition and rising cost. A key issue in the

3) The figure is ADB's (2005c) estimation of social protection coverage.

current debate on social security is its sustainability (Einerhand and Nekkers 2004; 40). Sustainability issue mainly relates with the present situation of many developed countries where existing system, operating on pay as you go basis, arranges plenty of services on almost universal basis requiring large amount of spending. Social security debate on developing countries emerged largely since 1980s (Guhan, 1994; 34) which primarily concerns with the expansion of coverage (both population and services). For expanding coverage, there are two options for developing countries: either expanding the coverage of existing schemes or introducing new schemes to provide necessary services to the excluded population.

International institutions and scholars have performed many studies on various aspects of social security. As a first comprehensive global examination on old age security, World Bank (1994) addressed the issues like how to maintain financial security of the schemes, what are the best ways for financing and how to share the responsibility between public and private sectors in order to enhance economic growth. The study, by identifying three functions (redistribution, saving and insurance) of old age financial security programs, recommended three-pillared system for "averting the old age crisis". Among three pillars, publicly managed tax-financed fist pillar is for guaranteeing minimum pension and other twos -mandatory privately managed self-funded pillar and voluntary pillar- are to enhance saving for self-support during retirement life. This approach emphasized individual responsibility for old age security by undermining the risk sharing and redistribution features that are commonly prevalent in most of the traditionally developed schemes, and emphasized the role of social security in promoting economic growth.

However, ILO and ISSA appeared in the opposition to the World Bank's strategy and hence WB's policy recommendation became controversial among the international institutions. The ILO and the ISSA opposed on the use of social security systems as a tool for capital market development and defended traditionally existed PAYG based defined benefit approach. The strategy of transiting from a public PAYG system to a private self-funded pillar is neither desirable nor necessary; rather it is very risky for future pensioners (Beattie and McGillivray, 1995). The writers, as the representative of

ILO and ISSA, mentioned that World Bank's study does not sufficiently attempt to make the reform measures consistent within the system and thus goes towards exacerbating the crisis in existing systems. Thus, controversy specially centered on the designation of fully funded mandatory second pillar. Subsequently, World Bank defended its stance by elaborating its intention and analyzing why the ILO and the ISSA came to different policy conclusions. While defending, James concludes policy differences on old age security is because the World Bank more concerns on the effect of social security in general economy, finds the existing system inequitable, believes behavioral responses and political economy factors sometimes make the design changes nonviable, and values risk diversification (James, 1996).

By now, greater consensus is apparent in social security realm on the realization of strengthening and developing protection policies and programs as an important measure for dealing with persistent poverty and rising vulnerability. The consensus has centered on 'social protection' as a framework covering a wider range of programs, stakeholders, and instruments in preference to alternatives such as 'social policy', 'social security', 'social insurance', or 'safety nets' (Barrientos, Hulme and Shepherd, 2005; 9). A wider consensus has also emerged inside and outside the World Bank including the International Labor Office, which was cautious in the past in designing a multi-pillar framework for retirement support (See, Gillion, 2000; World Bank, 2005). Thus, fierce debate has melted down and all agencies are now aiming at mutual understanding and, in particular, coordination and cooperation in developing schemes for social security in member or recipient countries. However, as there is no single right model of social security (ILO, 2001; 2), policy selection in a particular country should depend on existing institutional set-up and managerial feasibility, financial capacity and labor market structure, requirement of universalizing the coverage, and historical and social context. Above all, multi-pillar system is a better choice and there should be some sorts of government intervention in managing social security to prioritize its important objectives of poverty reduction, promoting equality and ensuring basic living standard, particularly in the context of developing countries.

Presently, despite of consensus on some fundamental aspects, different international institutions are working on social security with their own approach and principles. World Bank is working through social risk management approach that aims to provide instruments for enabling people minimize the impact of risk exposure and prepare themselves to be out of poverty and lower their vulnerability. It requires to look from more comprehensive approach which draws attention to many more risks, and which proposes many more instruments of dealing with diverse risks, than traditionally considered by social protection for making the social protection efficient in developing countries (Holzmann, Sherburne-Benz and Tesliuc, 2003; 1). Enhancing the coverage and effectiveness of social protection for all is one of the four strategic objectives of the ILO for which it emphasizes on its overriding concern of "promoting decent work for all". For ILO, social security is a key ingredient of its goal of decent work and recognizes it as a human right (ILO, 2001; 104). Through the social protection measures, ADB aims to reduce risks and increase opportunities for achieving its overarching objective of reducing poverty. It defines social protection to consist of policies and programs designed to reduce poverty and vulnerability by promoting efficient labor markets, diminishing people's exposure to risks, enhancing their capacity to protect themselves against hazards and interruption/loss of income (ADB, Webpage; 2006). These institutions are increasingly supporting both developed as well as developing counties through various projects for reforming existing schemes or introducing new plans as per country requirement.

Generally, social protection is considered wider concept than social security, however, in this study we do not distinguish these two terms in their strict meaning. Here, we often use the term social security as Nepal also uses the same term, and try to figure out future scope of the system based on country circumstances. While examining the policies for developing countries, Ginneken defines social security as "benefits that society provides to individuals and households- through public and collective measures - to guarantee them a minimum standard of living and to protect them against low or declining living standards arising out of a number of basic risks and needs" (Ginneken, 2003; 11). We also consider definition for this study purpose.

Although extending social security services to whole population is the preference for developing countries like Nepal, it cannot arrange every aspect of social security instantly even if it desires. Therefore, firstly, evaluating the present situation of the system in depth is important for shaping the future route of the system, which is major concern of this study. Though there are many studies on developing countries' context, no comprehensive study have been made covering all aspects of social security system in Nepal yet. In this backdrop, we vividly examine existing schemes for social security in Nepal, and discuss on needs and challenges in the country. In the following section, we examine informal practice of social security services, formal initiatives and policy framework, and general structure of existing social security schemes in Nepal. Third section deals with Employees Provident Fund (EPF) and Citizen Investment Trust (CIT) which are the contributory schemes operating in Nepal. Non-contributory schemes of social security- retirement benefits, elderly and disabled assistance and others- are examined in fourth section. After observing points on needs and challenges for strengthening future course in fifth section, conclusions and policy implication are made in the final section.

2. Evolution of Social Security System in Nepal

2.1. Informal Measures

Like many other Asian countries, communal and family support is the traditional means of social security that sustained in Nepalese society backed by social values, communal attachment and people's belief on religious matters. Guthi (community welfare trust) is one of the living examples among Newar (the dominant caste in the capital city) communities. Guthi system is a collective practice, which concerns on decent living standard of the members in a society, and is guided by the principle of solicitude. The main objective of the Guthi is to arrange welfare activities for the people by undertaking a religious activity such as installation of an idol of god or construction of a temple (Vajracharya, 1998). Guthi tradition is the evolvement of communal realization to live together, earn for one's livelihood, ensure one's life and work together for the benefit of every element in a society. Membership of a Guthi may be voluntary in some instances and compulsory in others and it entails a balance of privilege and responsibility among the members. In fact, because of people's deep concern on godly matters, Guthi's involvement in various religious activities encouraged individuals to participate in this tradition and helped to make communal bond tighter, warm, and consequently zeal of supporting each other expanded in friendly manner. Since its inception, more than 2000 years ago, the Guthi tradition has played a significant role in shaping and supporting the socio-economic development of Newar communities (Shakya, 2000). There also exists Guthi tradition at present but attraction is declining rapidly.

Similarly, there exist other diverse traditional arrangements in other ethnic or communal groups, which are generally aimed to support participant families against selected contingencies. Mutual support and social assistance occur in different form as stipulated in their understanding. Sometimes, such groups also accumulate small welfare funds to utilize in contingency cases. In overall, cultural/caste-based/community-based mutual aid and pooling of social funds, for fulfilling basic social goods, are important forms of informal social security services that assist each other through cash or in kind services. However, not all the communities meet all or similar set of contingencies. Collective responsibilities are often to help in funeral ceremony of a participant family, financially support in selected contingencies, uphold and preserve the values of important places and help to maintain social law and order. Nevertheless, the speedy process of globalization, wider practice of nuclear family system, widespread of consumerism and individualism are causing rapid weakening of such traditional means of support.

Besides the traditional non-institutional attempts, institutional practices emerged for providing social services since late 1940s in Nepal. As a communal attempt in 1947, Paropakar (Welfare), for the first time, established as a purely voluntary and philanthropic organization having objectives of protecting orphans and operating various educational activities. Similar, type of organization is Janakalyan Sanstha (public welfare association) established in 1965. In the similar fashion, ethnically motivated caste-based social institutions emerged from 1950s, which provided social services within selected communities and embarked for the welfare of deprived groups in their communities. Many welfare organizations also emerged in joint initiative of government and the communities with the spirit of performing social services. Examples are Nepal TB Eradication Association (1954), Nepal Blind and Disabled Association (1968), Nepal Leprosy Eradication Association (1970). However, over the time, traditional supportive measures are fading out or becoming less effective, institutional attempts are insufficient and hence government efforts through formal schemes are considered more important than ever.

2.2. Formal Initiatives and Policy Framework

Organized government effort to provide social security services operated started in 1934 when Provident Fund scheme came into existence with the establishment of Sainik Drabya Kosh (Army Provident Fund, APF). This scheme was initiated with the hope of removing financial hardship of army personnel after retirement. Under the scheme, army staffs were required to contribute by a specific percentage of their salary. A decade after the establishment of APF, Nijamati (Civil Service) Provident Fund (NPF) was established to collect savings from civil servants in 1944. Shortly after this, Employees Provident Fund department was established under the Ministry of Finance and Economic Affairs, entrusted with the management of both Provident Funds. The coverage was extended to cover entire government employees including police and teachers in later years. Pension system came in practice from 1930s covering only military people in the beginning.

In 1981, after visualizing the need to form separate ministry for labor and social welfare, government gave strengthened focus on welfare matters along with the formation of Ministry of Labor and Social Welfare. At present, welfare concerning ministry carries the responsibility of policy formation and planning regarding development and coordination of all activities related to women, children and social welfare. Government has introduced some new schemes recently and various programs operate to fight against poverty and social injustice, many of which explicitly or implicitly remain within the social security purview. In this manner, realm of social security has been gradually widening and diverting from informal measures to government-regulated organized institutions over the years. Nonetheless, social security, as such, has not gained due focus in government policies yet.

Community targeted welfare, empowerment and social development activities performed by NGOs and INGOs have flourished greatly since few decades back in Nepal. Consequently, for effective management and better utilization of non-government organizations, Social Welfare Council (SWC) was established in 1992 to look after the activities of such organizations as an autonomous body. After the establishment of SWC, NGOs/INGOs are required to take permission from the council and remain affiliated with it to operate their activities. NGOs, affiliated with the council are probable to receive government supports in the form of administrative help, training and cash grant.

Moreover, as the first labor act, Factory and Factory Workers Act was legislated in 1959, which was repealed by Labor Act of 1992. Only after the restoration of multiparty democratic system in 1990, trade unions activities became legal and they now work as a major pressure group for the establishment, extension and promotion of social security system. Recently, although local bodies are permitted to involve in social security and welfare activities, they are performing hardly any such activities in the lack of their own fund. Similarly, government has implemented social security program directives to regulate Allowance program in 2004. Because of the absence of competitive labor market, poor bargaining capacity of work force and high volume of informal economy, role of private sector (particularly by employers) in arranging social security services is not so significant. In summation, there is not much workout regarding social security from the policy perspective and steps that government takes further are hope for better designing of social security system in Nepal.

2.3. Basic Structure of Existing System

Two plans, Employees Provident Fund (EPF) and Pension were the only schemes of social security until 1990 and were generally taken as the special privilege to government workers than social security service, as such. Later, when the King's direct rule was overthrown by multiparty democratic system in the beginning of 1990s, government emphasized market economy and gradually realized the need of social security services, at least, for the elderly and incapables. In mid 1990s, allowance scheme for elderly, disables and widows was introduced that pays monthly cash benefits on flat rate basis to the defined categories. Similarly, although not with the vision of social security, Citizen Investment Fund, a voluntary saving scheme, is in operation aiming to contribute capital market development since 1990. This saving scheme has become a supplementary plan for accumulating and enhancing saving for upper income individuals. Providing social security is among its secondary objectives and deserves capacity to become second layer of social security for high-income people in long run.

Besides the major schemes mentioned above, government allocates budget for social assistance that mostly provides in kind benefits. Specially, government has strengthened poverty targeted small-scale programs in local communities in 1990s and onwards by announcing different schemes in national budget. However, because of political instability, centrally managed service delivery system and lack of proper integration among the programs they could not effectively reach to the poor and hence there was not significant reduction in poverty. Consequently, for directly reaching to the needy, government is now implementing new schemes which seem sustainable and comprehensive than the earlier ones. In this line, initiation through Senior Citizen Treatment Program and creation of Poverty Alleviation Fund are important.

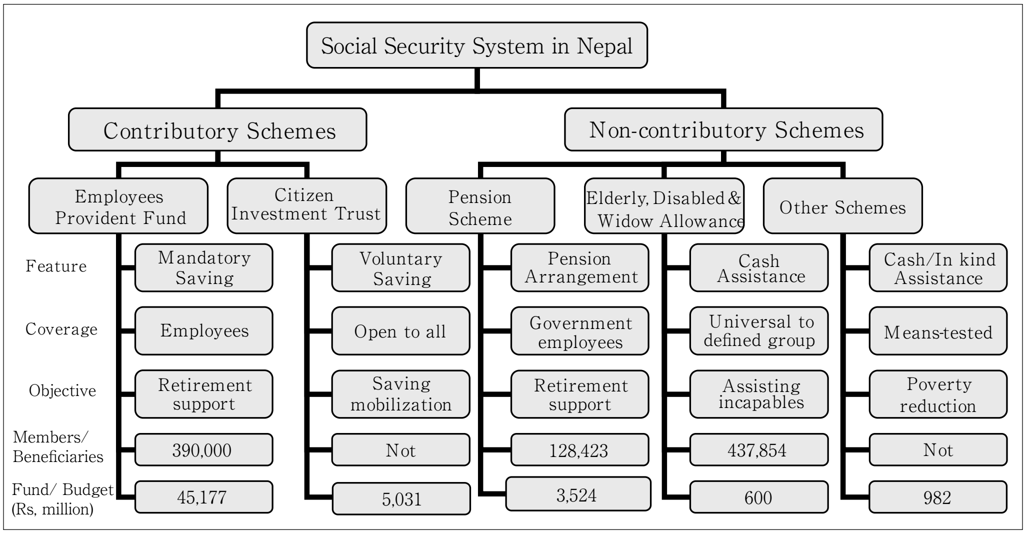
In Nepal, selected provisions regarding social security have been drafted in legal documents but their realization in practical life is poor, especially in private sector. Such provisions mostly confine within big business houses and sometimes only government sector workers. Except selected benefits for selected categories (especially for old people), most of the non-employees are practically untouched by the social security system. A survey of 425 enterprises conducted by a trade union (GEFONT, 2000), provides basic scenario on the provision of social security for 1990 and 1999 as shown in the table below. If we base on NLFS (1999) figure, there are around one and half million institutional employees, out of which twenty percent, who are mostly public sector employees, have significant coverage of social security. Employees of unregistered private organizations, that account 29 percent of total institutional workers in private sector, can hardly expect protection through social security schemes. These features clearly show that social security system as such is a relatively new phenomenon in Nepal. Importantly, most of the people can barely understand its basic principle and might be reluctant to contribute for the system, in general case. Despite of some progress in regulatory framework, it is yet to develop a comprehensive set of policy and give focused priority to social security in national level. Lack of comprehensive framework is not only the problem. Finding appropriate financing source, improving administrative structure and identifying the neediest people are other set of problem.

Table 1. Changing Scenario in Coverage Provisions in Enterprises, %

Provision	1990	1999
Provident fund	41	63
Gratuity benefit	34	50
Accident insurance	12	26
Sick leave	52	86
Maternity leave	23	47
Workmen's compensation	17	28
Housing facilities	37	76

Source: GEFONT, 2001.

Chart 1. Summary of Social Security System in Nepal



Above chart summarizes the schemes of social security, both contributory and non-contributory in Nepal. Two schemes, Employees Provident Fund and Pension, aim to support in retirement. Citizen Investment Trust is a voluntary saving enhancement scheme and primarily aims to contribute capital market development and makes only meager efforts to provide social security services until now. Senior Citizen, Disabled and Widow Allowance pays cash benefits on flat rate basis to the defined categories. Other schemes are mostly means-tested, temporary in nature and provide in-kind assistance to the poor. In the chart, budget size mentioned for "other schemes" is tentative spending on social assistance.

3. Contributory Schemes

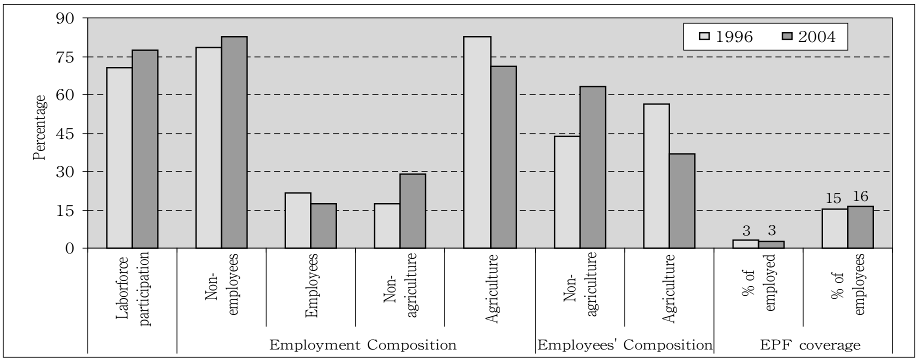
3.1. Employees Provident Fund

Employees Provident Fund (EPF) was formed in 1962 by combining then existing two provident funds and operates under the general supervision of finance ministry. In the phases of expanding coverage, lately from 1990, any business enterprise employing ten or more workers is allowed to register with the EPF, which accumulates monthly contribution from employers on behalf of respective employees. Since its establishment, EPF remains a major social security providing institution in Nepal. Nevertheless overall social security coverage remains very narrow with trifling effectiveness. Currently, contribution rate provisioned for EPF purpose is 20 percent, shared equally by employees and employers. Although government nominates all members of the EPF Board and makes important policy decisions in annual budgets, legally managerial body is autonomous in all aspects of management. As a social security scheme, all the contribution and withdrawal transaction made with EPF are free of tax and government guarantees three percent of minimum interest rate on the accumulated fund.

3.1.1. Employment Structure and Coverage

Although the large proportion of population is making survival in agriculture sector, labor force participation in Nepal is relatively high. Because of high dominance of agriculture sector and seasonal farming therein, unemployment rate is not so high but the rate of underemployment is surprisingly large. As revealed in living standard survey, 76 percent workers are engaged in agriculture sector and total underemployment rate was 46 percent in 2004. Most of the employed population consists of self-employed with very low proportion of employers. EPF Act makes mandatory provision for the government sector employees while it grants voluntary coverage for the employees in any institution with ten or more employees. This means, other workers either they are self-employed, domestic workers or part time workers are not permitted to take part in the scheme. Given the high dominance of self-employed people in the country, EPF provision itself keeps considerably large proportion of workers outside the coverage. Besides that, practice of informal business, either they are running as a family business or employ few workers, is quite common. As of 1999, around 73 percent of non-agricultural workers were involved in informal sector[4]. Thus, existing coverage provision is itself very limited. Moreover, due to voluntary provision of coverage, involvement of private sector workers in EPF is very low. Following figure provides a picture on employment composition and EPF coverage.

Figure 1. Employment Structure and the EPF Coverage in Nepal



Sources: Living Standard Survey 1995/96 & 2003/04, and EPF.

High rate of population growth and increasing life expectancy have jointly contributed large volume of labor force in the economy. Figures show, growth rate of

4) Report on NLFS 1998. Those who are not primarily involved in agriculture and work for the employers who employ ten or less workers and those who run such business are considered informal workers in the Survey.

employment (4.8) is much higher than that of population (2.3) for the period 1991- 2004. Certainly, starting only with selected government employees, EPF scheme has brought increasing number of employees into its coverage over the years. However, while looking from the proportion of employed population and total employees, there is not any significant progress over the decade.

3.1.2. Components of Employees Provident Fund

Retirement Support

Primarily, EPF is fund-managing institution for member employees that collects contribution from the corresponding employers on behalf of their employees. Primarily, it aims to support participants financially at their retirement life. EPF accumulates saving on personalized basis by creating individual account to each member and mobilizes the sum to provide interest return to its members on annual basis. As the foremost social security service, EPF pays the accumulated sum back to the members on lump sum manner at the time of job termination. Inherently, there is no redistribution of income among the members in the system because each member is entitled to receive the amount accumulated in their personal account. EPF had not any provision for pre-retirement withdrawal nor did it contain any additional social security services for a long time since its establishment. However, from early 1990s, it enhanced its scope by enlarging members' privileges and choices by arranging additional services to the members. Among them, some are explicitly social security services while others are cheaper loan facility to the members in need. For certain period, EPF had also permitted partial pre-retirement withdrawal to the members, which no more exists. Additional social security schemes and loan schemes are discussed below.

Additional Social Security Schemes

In addition to the retirement benefit paid on lump sum from members' personal account, EPF is paying funeral benefit since 1990 to support family members of the EPF members if death occurs while still being the active member[5]. The benefit amount as such is not so large (Nrs. Five thousand[6]). Similarly, introduced in 1995,

5) Active participants are those who are currently contributing to the EPF.

6) Monetary amounts presented anywhere in the paper are in Nepalese Rupee if no ↗

accident indemnity scheme financially assists members or their families against accident-caused disability or death of a member. EPF members or their family members are subject to a maximum lump-sum benefit of NRs. fifty-five thousand in the case of complete disability or member's death. All active participants are eligible for this benefit regardless of age or work nature. EPF had introduced periodic pension scheme that provides additional financial support to the retired members since 1996[7]. However, this scheme has lately been replaced by lump sum retirement benefit. In the new provision, retiring members who have contributed for at least 3 years over the last 10 years of service period can get a benefit amount equivalent to 0.75 percent of saving accumulated in their personal account offered at retirement multiplied by number of contributory years. EPF has run a special fund, reserve fund, generated out of its interest earnings to finance all these additional social security schemes. Members cannot expect large amount of benefits from these additional schemes. Nonetheless, as a social security scheme, this has contributed significantly without making any separate contribution for the same. Following table depicts increasing participation in various schemes.

Since the amount accumulated in reserve fund is created out of earnings of the members saving, it is in fact collective fund of the members. Among all the additional social security schemes, additional retirement benefit plan is the dominant component. Under this plan, the mechanism of fixing the benefit amount based on their personal accumulated sum encourages members not to withdrawal their saving before retirement. However, at the same time, benefit-fixing method favors those members who have higher propensity to save i.e. richer groups. Creation of collective fund to finance social services sounds good initiation but service provision requires modification if the Board really wishes to support the underprivileged groups favorably and enhance income redistribution.

↘reference is given. As of December 31st, 2006, 1US$ = 70.7 Nepalese Rupee and 1¥ = 0.59 Nepalese Rupee (Nepal Rastra Bank, Webpage).

7) Total pension amount paid every year is equivalent to five percent of the accumulated sum at the time of retirement. Over the past eight years, number of beneficiaries increased by five times and so is the trend of per capita benefit. Further, the benefit that members are receiving is increasing in proportion of per capita GDP in national level.

Table 2. Participation Rate in Different Schemes of the EPF

Description	2003	2004	2005
Fund withdrawal	6.8	6.9	7.6
Loan schemes	19.8	20.6	24.2
Additional schemes	3.2	3.1	4.2
Total participation rate	29.9	30.6	36.0

Source: Kosh Samachar, various years, EPF.

Presently, with only limited coverage and having no income redistributing measures in the system, EPF is not contributing in poverty reduction or promoting equality, which are the major objective of the social security specially in developing countries. The system in fact is working as a special privilege granted to the organized sector workers. To make low-income people benefit, EPF can also consider members' income level to fix benefit amount rather than considering only accumulated personal sum. Such changes in the system will keep on encouraging members to save more for retirement and enhance income redistribution. Currently, collective/pooled sum of the EPF is around seven percent of the total EPF saving. This large amount of fund pooling has high potential to introduce redistributive elements in the EPF. Similarly, these additional schemes are also showing the feature to move towards the pay as you go based financing method while building intra and intergenerational solidarity and integration as reflected in the collective nature of the fund. Thus, with some modification, it is possible to introduce some elements of PAYG financing and minimize the financial risk of fully funded scheme.

Loan to Members

Loan facility to the members was started from the special loan scheme in 1994 and presently EPF has additionaly provides loan for housing and educational purpose to its members. Rate of interests are cheaper than the market and withdrawal provisions have been made easier over the years. Unlike in other two loan schemes, members are not required to deposit collateral for special loan and interest rate is much cheaper. Under this scheme, members borrow certain percent of their personal saving. Housing loan was introduced in 2000 so as to assist members build personal residential house but it support to build houses only selected area. As the percentage of people residing on their own house (91.6% in 2004) is falling in Nepal, this scheme is compatible with members need and there is increasing attraction in this scheme. Education loan is the newest scheme under which members can receive loan to finance higher education of themselves or their spouse or children. EPF initiation to involve in real estate business motivated by the objective of both saving mobilization and enhancing security services.

3.1.3. Members' Saving and Operational Efficiency

Because of the self-funded scheme, accumulated saving of members is a major asset for the EPF to arrange social security services. Because of increasing number of schemes and investment returns realized in the fund, accumulated sum is increasing continuously. In fact, EPF has developed as the largest financial institution in the country from the viewpoint of capital accumulation and mobilization. In the table below, we can notice that over the last decade, total accumulated fund increased by more than five times and exactly same rate of growth can be seen in per capita EPF saving. Both yearly contribution and accumulated saving, in percentage of gross domestic saving, have significantly increased to be 6.9 and 65.1 respectively in 2004. Significant growth in saving can be realized in terms of other national variables as well. Per capita EPF saving is much higher than the per capita GDP growth as reflected in the saving GDP ratio. Accumulation of saving can also contribute to overall growth of the economy by promoting financial market, in addition to social security benefits to the participants.

All the managerial expenses of the EPF are financed from its own earnings i.e., investment returns in the accumulated fund. Therefore, managerial efficiency of the

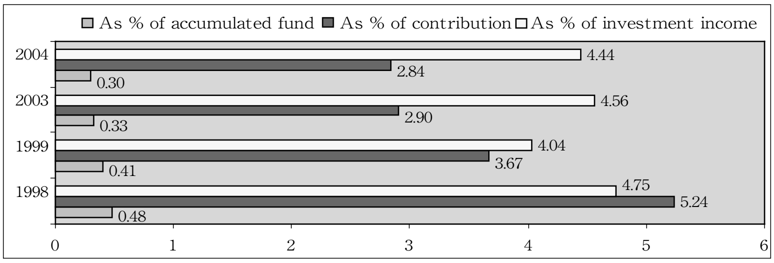
Table 3. Performance of the EPF compared to Relevant Variables

	1994	1998	2001	2004	2005
Accumulated fund (million)	8,239	16,455	25,871	40,209	45,177
Yearly contribution (million)	1,112	1,512	2,444	4,241	-
Per capita saving	26,579	53,082	83,453	129,706	145,732
Accumulated Fund as Percentage of					
Gross domestic product	4.3	5.7	6.6	8.5	9.0
Total govt. expenditure	24.5	29.3	32.4	45.0	44.8
Domestic saving	28.1	39.7	41.8	65.1	69.6
EPF Saving/GDP (per capita)	2.6	3.8	4.7	6.5	7.1

Sources: Economic Survey, 2005; EPF.

autonomous social security institution directly relates with the benefit package it can provide to members. Shown in the figure below, managerial cost of the EPF is decreasing rapidly. Administrative expenditure has significantly reduced in percentage of both annual contribution and accumulated fund. EPF has gained efficiency along with the rise in fund size, computerization of the management system and retrenchment of abundant jobs. With the larger number of members and increased fund size, EPF has possibility to manage the fund in much cost-effective way in future.

Figure 2. Managerial Efficiency of the EPF



Source: Kosh Samachar, various years, EPF.

3.1.4. Investment Policy and Performance

Since members' cannot withdraw their saving before retirement for any purpose, EPF is the sole body to mobilize collected fund and provide returns. Investment policy 2004 provides guiding principle regarding the investment of the accumulated saving. To mobilize the sum, first priority is apparently given to service-oriented loan to members in the recent years. Other investment instruments are government bonds, bank deposits, housing and real estate, project loan, and share and debenture. For diversifying investment risk, maximum limit is fixed for each investment alternatives. Maximum limit provisioned for investment is the highest for contributors' loan (60%) followed by bank deposit (50%), government bonds (30%) and 25 percent is fixed for each of the rest choices of investment. There is no provision for investing the amount abroad.

Following table shows the composition of investment portfolio. Almost entire accumulated fund has been mobilized by the EPF over the years. Fixed deposit with commercial bank got the largest proportion in investment portfolio until 2004 while loan to contributors topped in the latest year. Volume of loan to contributors has escalated in recent years. There are two fundamental reasons behind the rise of loan in this component. Firstly, due to economic slow down in the country, there are less opportunities for the EPF to mobilize its fund so it is encouraging members to borrow with liberal options. Secondly, decreasing returns on accumulated saving and falling interest on loan (i.e. smaller difference between receivable and payable interest rate) encouraged members to borrow more and invest in alternative means.

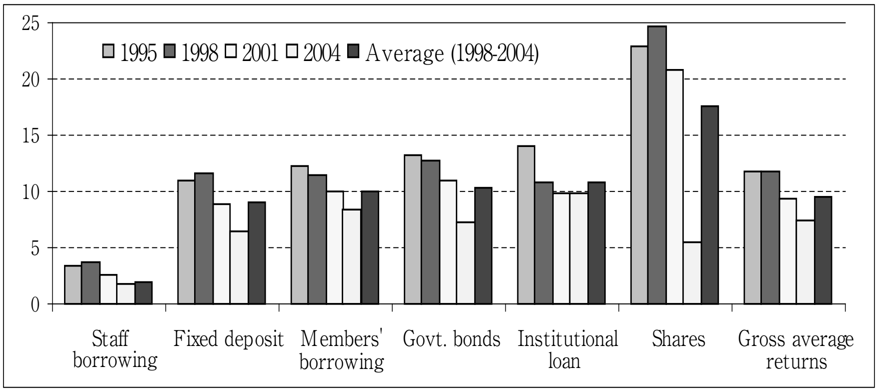
Table 4. Portfolio Composition of the EPF, in Percentage

Category	1973	1995	2001	2005
Government bonds	18.7	30.8	11.9	11.0
Bank deposits	58.4	57.1	60.2	35.0
Institutional and other loan	3.3	4.2	11.7	12.0
Loan to contributors	19.6	6.3	14.5	38.5
Others	0.0	1.7	1.6	3.5
Total	100	100	100	100
Total (% of accumulated fund) na	95.8	95.5	98.2	

Source: Compiled from Kosh Samachar, various years, EPF.

Over the years, institutional loan is also increasing. Others, which are loan to staffs and investment on share and housing project, have remained minimal for the entire period. Thus from 88 percent of mostly risk-free and administratively easy investment allocation (investment in government bonds and fixed deposits) in 1995 has declined to 46 percent in 2005. Despite the positive change, investment still concentrates on fixed interest yielding instruments. There is not much scope to continuously depend on such instruments because EPF already has dominant share on both government bonds and fixed deposit with commercial banks. Therefore, EPF needs to find more sustainable investment alternatives presuming that loan scheme cannot continuously attract members. EPF has legal right to fix the rate of returns that it provides to members' saving in its own forethought. First calculating the total income, it fixes rate of returns to members after allocating necessary amount for administrative expenses and reserve fund. Returns realized in various investment instruments are presented in the figure below.

Figure 3. Returns Realized in Different Investment Instruments



Note: Yearly investment return for is calculated by using the formula

$$r=\frac{I}{(SI+EI)/2}x100$$

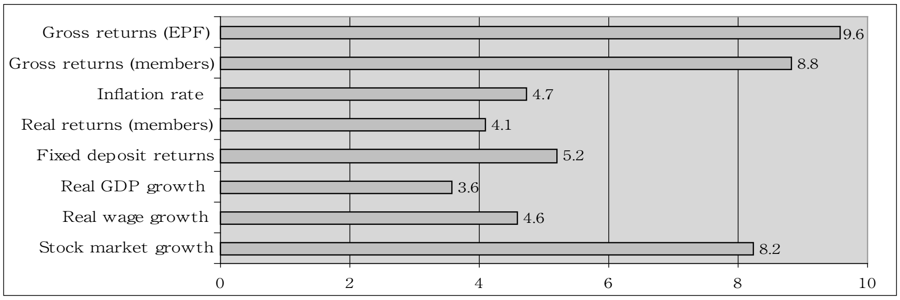
where I, SI and EI respectively refer to interest income of the year, starting investment allocation and yearend investment allocation. Average returns for 1998-2004 is arithmetic mean of the yearly returns.

Source: Kosh Samachar, various years, EPF.

From the figure, we can note that rate of return, on average, is falling in all investment instruments. Loan provided to staff members has yielded the lowest returns. Due to the small sum allocated in this item, it makes little sense to overall returns of the fund. Nonetheless, low rate of returns on staff borrowing has greater meaning if we compare it with the returns on members' borrowing implying greater privilege provided to staff members than the contributors. Fixed deposit with commercial banks has the second lowest investment yield whereas it always got the highest investment allocation during the period. Returns on members' borrowing and government bonds are attractive than that of fixed deposit. Returns yielded by institutional loan and shares are the highest ones despite of economic slow down in the country. Unfortunately, most fruitful instruments got lesser investment allocation.

The above figure presents EPF's investment return and growth in selected macro variables. For the period 1998-2004, inflation, as measured by the change in implicit GDP deflator, averaged at the rate of 4.7 percent that reduced real the returns to be only 4.9 percent (4.1 percent to members). Still, on average, real return granted to

Figure 4. Investment Returns of EPF and Growth in Selected Variables (1998-2004)



Note: Stock market growth is measured in terms of growth in composite index calculated as an average of market capitalization ratio (to GDP), ratio of turnover to GDP, and turnover ratio (to market capitalization). Growth rate of stock market and wage is respectively for 1997-2005 and 1999-2004 period.

Sources: EPF, Economic Survey 2005, NRB, Living Standard Survey, ADB, 2005a.

contributors is higher than the overall economic growth rate but less than aggregate fixed deposit returns in the country. In the burgeoning economy, despite the worsening economic situation in recent years, performance of financial sector, as measured by growth of composite index of stock market, is overwhelmingly high in comparison to overall GDP growth. Comparative figures reflect on the possibility of providing higher returns to members by investing the fund more prudently.

Summing up the section, the most notable aspect is that despite the oldest and largest social security scheme in Nepal, EPF has only stringent coverage. Moreover, until early 1990s, EPF remained simply a mandatory saving plan that paid lump sum benefits at retirement for government sector employees. However recently, in addition to lump sum retirement benefits, EPF has introduced additional schemes have been introduced and members' saving is increasing rapidly but no arrangement has been made for ensuring health service access. In a decade, from 1994 to 2004, EPF fund, as percentage of domestic saving, has become more than double and per capita EPF saving to per capita GDP ratio has increased by around three times. Currently, in addition to lump sum retirement benefits, members can benefit through loan schemes and social security schemes like accident indemnity, funeral grant and additional retirement benefit. Due to growing competitiveness in financial market, EPF returns are falling, requiring more prudential and competitive investment disbursement.

3.2. Citizen Investment Trust (CIT)

Citizen Investment Trust, established in 1990, is a single investment trust in Nepal which by now accepts saving from both individuals and institutions on voluntary basis. Besides ten percent of government share, this semi-government institution has shares of the central bank (40%), Stock Exchange Limited (10%), bank and financial institutions (20%) and individuals (20%). The Board consisting of government nominated maximum of seven members regulate the Trust reflecting direct influence of the government in its management. Primary objective of CIT is to mobilize scattered savings in medium and long-term investment and provide services of financial intermediation[8]. Fundamentally, it is not a social security providing institution as its corporate mission is "to enhance investment opportunities and promote capital market by encouraging ordinary people to save for the ultimate objective of economic development". Nevertheless, it encourages individuals to save for contingency needs and supports by mobilizing accumulated sum. Recently it has initiated social security schemes like retirement fund, pension schemes and insurance however their effectiveness is very limited. Thus, overall contribution of the CIT lies in terms of saving and investment mobilization, capital market development and expansion of social security coverage to the individuals. CIT, through the mobilization of accumulated fund, pays interest returns to members' deposit after allocating its operating cost.

3.2.1. Various Schemes of CIT

Employees' Saving Growth Scheme (ESGS) is the first scheme operated by the CIT which accepts voluntary contribution from employees through respective employers at a rate of 5 or 10 percent of salary for a period of ten years (it was five years before 1998)[9]. Some forty thousand individuals were participating by the end of 2002; no exact data is reveled for recent years. Employees can join this program any time but have to

8) The Trust additionally aims to provide services of issue management, underwriting, bridge financing and consortium financing to the corporate sector from which it seeks profit to the shareholders.

9) The scheme, in the beginning was mandatory for all institutional workers, which was made voluntary just after few months of operation. According to a senior staff in CIT, this scheme originally has implicit objective of controlling possible escalation in inflation as salary of government employees was raised considerably by then.

wait for pre-specified period to make the statuary withdrawal. Participants can also borrow against their accumulated assets for the sole purpose of investing in securities promoted by CIT. Average rate of return was 6 percent in 2004. Rather than social security, this program is specifically for saving mobilization purpose.

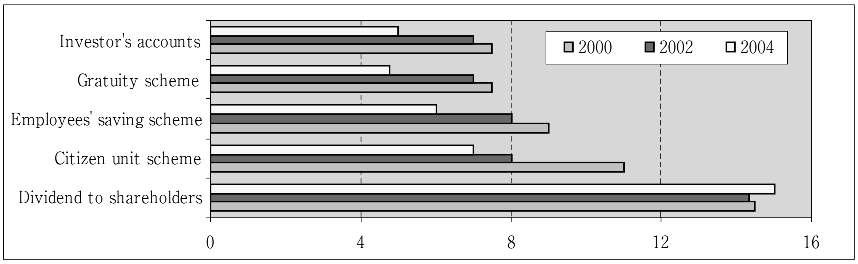
Citizen Unit Scheme was introduced in 1995 to provide option for every individual to accumulate saving in an organized form and mobilize saving in institutional form. Trust issues units of Rs. 100 which any individual can purchase in the quantity of ten and multiple of ten. Institutions can also buy such units, however at larger volume (not less than 5000 units). Participants will be paid benefits in the form of dividend, annually. Unit holders can also sell the units back to the issuer at any time. A maximum of ten thousand is subject to tax exemption including returns gained therein for each participant. Number of participants in this scheme was nearly seven thousands as of end 2002.

Investor's Account Scheme is a retirement scheme operating through voluntary contribution from individuals, since 1999. It is not tax exempted, however does not pay withholding tax too. Participants cannot withdraw their accumulated fund in this scheme prior to retirement when they receive lump sum payment. Around nine thousand individuals were participating in the program in 2000; no recent data is available. CIT is also managing pension/gratuity scheme from 1999, which aims private companies participate in the scheme and contribute on behalf of their employees. Participating companies voluntarily accumulate saving to arrange defined benefit pension for their employees. CIT is liable to mobilize the saving and pay higher possible returns to the participants. Besides these schemes, CIT, from 2005, has started to manage the fund of government employees (only civil service workers at present), as per the government decision to replace existing non-contributory pension system by contributory one. Further, government has provided the responsibility of managing the insurance fund of government employees by making it contributory. Thus, the scope of CIT is widening gradually as a social security providing institution.

3.2.2. Saving Mobilization and Returns

Total fund accumulated with the CIT was not so large, less than one percent of both government expenditure and domestic saving, in 1999. However, it is increasing rapidly; total accumulated fund reached six percent of domestic saving in 2004. In 2005, total CIT fund is 11 percent of the total saving accumulated with EPF. However, out of the total fund accumulated with CIT, more than two-third is just for saving mobilizing purpose and remaining small sum is for retirement planning i.e. under Investor's Account and Gratuity Scheme. CIT In total, government bonds and others instruments yielding fixed returns share more than 74 percent. Rate of interest granted to different schemes differ as shown in the figure below. mobilizes accumulated fund of different schemes with different priorities. Social security targeted schemes- Investor's Account and Gratuity- have realized low returns because of less risky option chosen them. Rate of return is declining in all the schemes while there is not any significant change in dividend rate realized by the shareholders. This shows that CIT prioritizes shareholders' benefits at top priority.

Figure 5. Rates of Return to Participants and Shareholders



Source: Citizen Investment Trust, annual reports, various years.

In summation, despite of some initiation taken in arranging self-funded social security benefits, it mainly remains a scheme for developing capital market. Neither there is any mechanism for pooling risk nor is any guarantee provided for minimum returns like in the EPF. However, it deserves good potential to become a second layer of social security by enhancing voluntary saving and enlarging the schemes of social security in future. After all, this can be a scheme of attraction for high-income individuals to enhance saving in tax-exempted manner that supplements other major social security scheme.

4. Non-contributory Schemes

4.1. Pension Scheme

In addition to benefits receivable under EPF, government sector employees are subject to pension or gratuity, allowances and accumulated leave payment at job termination. Started from the military personnel in 1936, pension scheme expanded gradually to cover all government sector employees. Standard retirement age presently fixed is 58 for civil service workers while different provision has been made for workers in other sectors. For teachers, it is 63 years of age whereas lower ranks of military and police may retire as early as 46 - 48 years of age. Required vesting period to receiving pension is 20 years for civil service workers 16 years for military and police personnel. Annual amount of pension is calculated using the following formula.

$$\text{Annual Pension Amount} = \frac{\textit{Total Year of Service x Amount of Salary Last Drawn}}{50}$$

For high-level officials in military and police service, denominator value is set 40 to allow higher benefits to them. However, for all government employees, pension amount shall not be less than half of the starting salary of the incumbent nor more than hundred percent. There is not any mechanism to adjust inflation in the pension amount besides considering two-third of increase in salary scale for pension calculation purpose. Those workers terminating job before they are eligible for pension can get gratuity subject to a minimum five years' service they have offered.

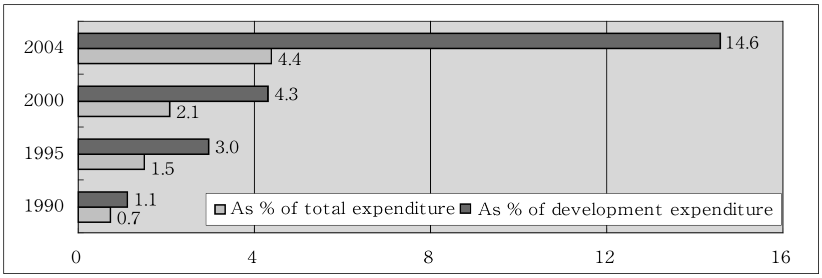
Total 5. Pensioners and Sector wise Distribution

Pensioners in Different Category, percentage	2002	2005
Civil servants	29.1	29.8
Police	20.9	21.5
Teacher	9.2	8.4
Army	36.0	35.7
Others	4.9	4.7
Total Pensioners		
Number	98242	128423
Percentage of institutional employees	7.4	8.0
Percentage of total employed	1.0	0.9

Source: Kaushi Toshakhana, and concerning offices of respective institutions.

In addition to government employees, few banks and public corporations also provide pension to their employees but there is no specific set of provisions. In total, number of pensioners is not so large (less than one percent) while comparing with total employed population. Out of total pensioners, military personnel, who are first category of workers eligible for pension, share the largest percentage. Civil servants and police jointly constitute around fifty percent while some nine percent are teachers. Despite of the small number of pensioners, retirement cost considerably high and escalating rapidly as shown in the figure below. For last fourteen years, total retirement cost increased by 25 percent of annual compounded rate.

Figure 6. Retirement Cost as Percentage of Government Expenditure



Source: Economic Survey, various years, Ministry of Finance, Nepal.

Due to increasing burden caused by relatively small number of pensioners, Nepalese government took a bold step in 2005 to replace the existing pension system, financed on pay as you go basis, by a contributory one. Under the new provision, in addition to ten percent monthly salary of civil sector workers (for those hired on and after 2005), government will make additional equivalent contribution from its general revenue to create pension fund. Currently, this new provision is applicable to only civil service employees and government is planning to extend it all government employees. This new system seems to develop in a way that Employees Provident Fund is operating at presently, however paying the benefits on yearly basis. Obviously, such change in existing pension system is not to extend coverage of social security system in the nation but to cut the burden of pension expenditure. Since there is no central authority to arrange pension benefits, concerning ministerial bodies are managing pension benefit for respective retirees. This has caused unnecessary burden and inefficiency in planning matters and benefit distribution process. Conversion into the contributory system will reduce government burden on social security but cannot perfectly eliminate double benefit arranged to the government sector employees. From long run perspective, it is essential to integrate EPF and public pension system for making social security system fair and less burdensome.

4.2. Senior Citizen, Disabled and Widow Allowance

In 1996, Nepalese government introduced a program for helping elderly persons aged 75 and over by proving monthly allowance of Nrs. 100. After one year of program instigation, coverage was expanded to helpless widows aged 60 and above, and disabled aged 16 or above. Allowance amount for senior citizen was also raised to 150 in 1999. Despite the universal coverage provisioned to the defined category, if we base on the statistics of population census 2001, beneficiaries under elderly and disabled allowance are respectively 66 and 4 percent of the defined category. Again through 2004 budget speech, allowance amounts have been increased form 150 to 175 for senior citizen, 100 to 175 for disabled and 100 to 125 for widows. Further, widows whose husbands are died in conflict are subject to allowances regardless of age limit. The effective annual benefits paid as such is not so high- only around 2/5th of the monthly salary of an average employee in the country. But the scheme has become an attractive because of its flat coverage and capacity to reach local and underprivileged people as well universally.

Table 6. Senior Citizen, Widow and Disabled Allowance: Coverage and Benefits

Year	Beneficiaries	Disbursement (Million Rs)	% of govt. expenditure	Per capita benefit (Rs)	Benefit as %of Per capita income
1996	346874	280	0.60	807	7.0
2000	385602	530	0.80	1374	8.7
2004	437854	600	0.67	1370	7.2

Source: Unpublished source, Ministry of Local Development and Economic Survey, MOF, Nepal.

Because of its flat coverage, even the people not in real need are benefiting in the scheme. A combination of a low benefit amount and high eligibility age makes the scheme less costly requiring only a small percentage of government spending. However, in the Nepalese context, priority is requiring to in kind services targeting local areas or communities where poor are concentrated. Similarly, government spending on poor targeted income-generating activities is much important for the betterment of the poor from the long-term perspective. There is also consensus on the need of skill development and opportunity creation programs so that poor can have access to vocational jobs and can be more self-dependent.

4. 3. Other Schemes

4.3.1. Social Assistance

Especially for uplifting the living condition of underprivileged people, women and children, there are different programs launched through Ministry of Women, Children and Social Welfare. Many of such assistive programs target specific areas or communities however, the schemes are mostly temporary in nature. Frequent change of government, budget constraints and poor effectiveness of the program are the reasons that make the program terminate shortly. Usually such programs provide benefits on means-tested basis but operate on central regulation, causing less effectiveness to reach the neediest people. However, attempts have been made for making the programs sustainable and support in fulfilling basic needs of socially and economically backward communities. Recently introduced scheme, Senior Citizens' Treatment Program, aims to assist those aged above 65 for meeting health services by providing a medical grant. Under the scheme, government pays maximum of Nrs. 4,000 to a person in a year. Presently its coverage is limited in selected areas.

Besides the assistance granted from the welfare concerning Ministry, other Ministries concerning with local development and labor also launch programs related to social security which are usually poverty targeted. However due to the poor performance of many centrally managed poverty targeted programs, Poverty Alleviation Fund (PAF) was established lately as an autonomous institution through its own Ordinance in 2004. It aims to ameliorate the situation of lower strata of the society mired in absolute poverty through targeted programs. PAF plans to operate programs through the fund received in the form of subsidiary grant from government and international development partners. The Fund has already started its activities in close and active collaboration with poor and deprived people in local areas by mobilizing them in the form of communities. PAF promotes demand-led Community Driven Approach using rigorous social mobilization by organizing and bringing poor at the mainstream of development. It encourages for the formation of community organizations and capacitates them for the effective and efficient implementation of projects. Within the period of two years, there are 1,137 communities associated with the PAF by early 2006. In the ongoing budget, total fund allocated for the PAF is 1.25 billion rupees which is 0.87 percent of total budget size of the year. Notwithstanding such various efforts, performance on poverty reduction and capacity development is rarely assessed and no significant changes have readily seen among the local residents.

4.3.2. Additional Benefits for Army Personnel

There are some additional schemes for military people and their families. Such schemes are like education of army children, medical coverage for soldiers and their families, housing schemes, legal assistance, micro-insurance, special programs for widows and family members and interest-free loan facilities. Large part of the fund accumulated by partial deduction of the benefits army personnel receive in returns to their service under the UN Peace Keeping Mission. There is blame on non-transparency of the fund and details of the fund was made public in 2006 for the first time. Various schemes have helped army people via financial as well as moral upliftment without burdening much to the government. Under the scheme of health support, parents and children of army personnel, either service holder or retired, will be treated free of charge in selected hospitals. Currently, all the army people are compulsorily insured in retirement benefit insurance, accident insurance, residential insurance though the benefit amounts are not so high.

4.3.3. Non-government Organizations

Many non-government organizations are also contributing significantly in the area of social and community development. Although such programs do not explicitly constitute the integral part of social security system, their role is noteworthy. Most of the services rendered by such organizations remain within the purview of social security system in all but name. Like the social assistance programs of the government, programs launched by NGOs are usually community targeted and aim to uplift the living standard of backward people. There are thousands of non-government organizations originated within the country however no accurate data is available regarding their financial situation. Similarly, role of the international NGOs is increasing in recent years. In the year 2005, total amount spent by INGOs on various sectors through projects stood more than three percent of total government expenditure. Health and community development is the objective taken by most of the organizations and total spending on this area is 68 percent of their total spending. USA and Germany are the largest contributors in terms of total spending while UK and Japan rank behind USA in terms of project number. Projects are concentrated in rural areas and target vulnerable groups in local communities. Possibility lies to coordinate with non-government bodies to make the spending on social security much effective for upgrading the living condition.

In summation, social security coverage of non-contributory schemes, in general, is confined to government employees and elderly population. Specifically, two major schemes of non-contributory type concentrate on old-age support, and Army Welfare Fund is strictly limited within the army circle. Out of various assistive schemes, most noticeable is again to assist old people to meet health services. Many assistive schemes aimed for poor population are less effective to reach the neediest ones and provide negligible benefits to eliminate their plight. Introduced in 2004, Poverty Alleviation Fund aims to assist poor by mobilizing the communities; its coverage is limited and effectiveness is yet to see.

5. Needs and Challenges Ahead

There is vast difference between social security concern in developing and developed countries since the existing institutional setting and financing capacity, nature of social problems and level of economic development differ. While looking from the social security perspective, developing countries have many features that pose problem in implementing the system. Importantly, weak financing capacity, dominance of unorganized labor market, poor administrative setting, social conflicts and political instability generally characterize low-income developing countries. Currently, fundamental concern on social security is to extend its coverage to greater number of people in the developing world. However, its comprehensiveness should depend on the severity of social predicament and financing or managing capacity of the government and public in a particular country. In developing countries' context, extension can have special implication to capture basic needs of the people going beyond the contingency requirements (Kannan, 2004; 7) and promoting people's capacity by shielding through the policies of physical capital, moving a step forward from human capital (Justino, 2003; 8). Rather than the service adequacy to selected groups, a minimum level of service for all is important.

Expansion of social security coverage to the whole population is also necessary for realizing better effectiveness of the system. Unless schemes cover everybody or nearly everybody, and they start to work properly, their effectiveness is limited (Gillion, 2000; 40). Guhan (1994) stresses that social security in poor countries will have to be viewed as part of, and fully integrated into, anti-poverty policies, providing access to productive assets, employment guarantees, minimum wages and food security. The most important objective of social security for the low-income countries is to reduce poverty and help in maintaining minimum living standard to the greater population. At the same time, policies should be compatible with the development needs of the country. Shown in the table below, Nepal unfavorably ranks on different aspects of social protection among the selected developing Asian countries. First ever-calculated indicators and index show small spending, limited coverage and weak poverty targeting in Nepal. This also shows increased concern needed on social security in Nepal.

Table 7. Social Protection Index for Selected Developing Countries

Countries	Composite SPI	Social Protection Indicators			
		Expenditure	Coverage	Poverty targeting	SP impact
Mongolia	1.0	1.0	1.0	0.8	1.0
Indonesia	0.6	0.2	0.6	1.0	0.5
Viet Nam	0.5	0.3	0.5	0.7	0.6
Bangladesh	0.4	0.4	0.2	0.5	0.7
Nepal	0.3	0.2	0.3	0.4	0.3
Pakistan	0.1	0.2	0.2	0.1	0.1

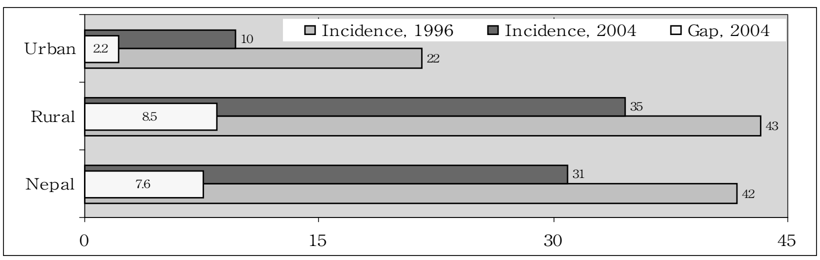
Source: Halcrow Group Limited, 2005.

From the discussions in earlier sections, we have found that, in spite of the various schemes existing in Nepal, they meagerly cover limited services for insignificant portion of labor force. The fundamental scheme, EPF, confines to organized sector employees. CIT, which has universal coverage but not fundamentally a social security scheme yet, attracts only upper income people. Government sector retirees, who are liable to receive pension or the gratuity, are also EPF participants. Further, government sector employees are probable to benefit once again under the scheme for elderly in their old age, resulting into multiple benefits to the same stratum. Thus, coverage of social security system in Nepal is one-sided; especially it favors government workers with the implicit objective of income maintenance. Noticeably, health services are virtually neglected in the overall arrangement existing at present.

5.1. Needs of Social Security System

Nepalese economy severely suffers form poverty, inequality and underemployment. The nature of poverty is complex and causes are diverse. Not only economic factors are responsible for high poverty and inequality but also social injustice that is enshrined on social values and traditional creeds is equally visible. Poverty is virtually a rural phenomenon with around 95 percent of the poor living in rural areas mostly making survival in agriculture sector. Poverty has sustained in Nepalese economy as the root cause and the most striking problem for the development of the country as a whole (see, JICA 2003, NPC 2002). Poverty has usually become overriding concern in planning documents deserving priority in the development objectives since Sixth plan (1981-1985). Particularly, Eighth (1992-97) and the Ninth (1997-2002) development plans kept poverty alleviation as their major objective, while it was sole objective of Tenth plan (2002- 07). The set of strategies reported in the Tenth plan constitute high, sustained and broad economic growth, development of social sector and rural infrastructure, targeted programs and good governance.

Figure 7. Poverty Incidence and Poverty Gap Index (PGI) in Nepal



Source: Central Bureau of Sstatistics, 2005.

Since the early 1990s, government implemented various targeted and sectoral poverty alleviation programs. However, such programs received scant participation in local areas due to centrally run planning and implementation process causing virtual ignorance of real preferences of the poor (see ADB, 2002). Lately published living standard survey reveals considerable decline in poverty (see figure below) but people's living standard has hardly been improved in effect. Survey finds remittances as the major contributory factor for reduced poverty. After all, notwithstanding the fall in poverty, there is more than one-third rural population surviving in poverty and poverty gap is still high as shown in the figure below.

Since PGI is based on the average consumption shortfalls of the poor, larger the gap between poor and non-poor in Nepal implies large amount of resource requirement to pull the poor population out of the poverty. ADB's study (ADB, 2005b) on social protection systems in six developing member countries reflects that three South Asian countries, where poverty is a particularly severe problem, are also the countries with the lowest social protection expenditure as a share of GDP. This implies that social security schemes have direct connection to poverty reduction efforts. A striking feature of the poverty reduction strategy papers is that none of the strategies make the connection between social protection and measures to ensure that poor people benefit from economic growth, implying that social protection is not seen as one of the tools for redistribution and development (United Nations, 2003; 59). Reducing poverty and inequality are among preferred development goals in Nepal necessitating the establishment of comprehensive social security system. Similarly, though the figure of unemployment is not so high, underemployment remains substantial. Underemployment is 46 percent while there is low productivity of workers. Even after prioritizing liberalization policies, private sector could not consume abundant labor force in agriculture sector. Although there number of factors contribute for low productivity in Nepal, lack basic social security services is one of the important.

Besides poverty and underemployment, high inequality is reflected in Gini coefficient, 0.41 in 2004. Similarly, inequality is not only high in terms of income but also in regards to people's access to the goods of basic needs and infrastructure. In the following

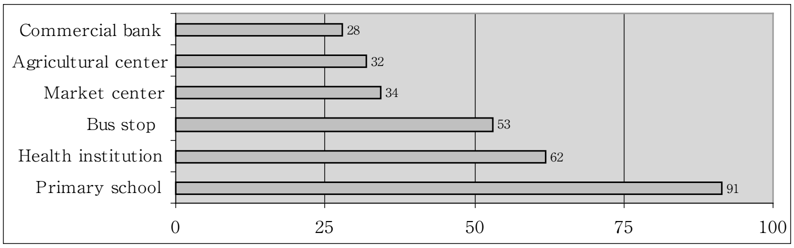
Table 8. Value Added per Worker by Sector (Constant, 2000 US$)

Countries	Agriculture	Industry	Services	Year
Nepal	270	1,061	1,292	1998
India	432	1,602	2,039	1999
China	530	4,351	4,133	2000
Indonesia	662	4,612	1,692	2001
Pakistan	1,001	2,322	2,826	2000
Malaysia	4,647	15,271	7,929	2000
Singapore	16,384	54,957	35,748	2001

Source: ADB, 2005.

figure, we can see large percentage of households traveling more than thirty-minute to access basic facility. As the facilities are centered in cities and large numbers of people live in rural areas, percentage of population having poor access to the goods of basic needs is high. Poor access to social-economic infrastructure has become barrier to widen capacity and realize their real potentiality for substantial population in the country.

Figure 8. Households Accessing Facilities within 30 Minutes, 2004, %

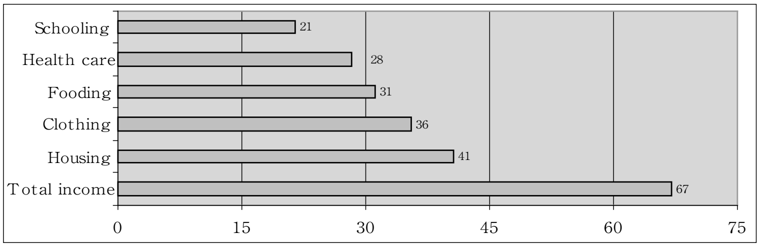


Source: Central Bureau of Sstatistics, 2005.

Similarly, living standard survey has shown that 67 percent people have less than adequate income (self-reported) to meet the services of basic needs namely, food, housing, clothing, health care and schooling. Around two-third households do not have adequate access even to the goods of basic needs like health services, food and clothing (see the figure below). In the absence of the sustainable and effective social security programs targeted to poor and vulnerable people, living condition of low-income people usually in rural areas has meagerly improved over the time. Large part of social security expenditure goes for paying pension to the retirees in government sector.

Contradictorily, the neediest population is virtually untouched by the schemes. Thus, needs of social security lies on poverty reduction, income redistribution, enhancing productivity and supporting people to meet basic needs and enhance development pace.

Figure 9. Inadequacy of Basic Needs, 2004 (Self-reported, % Households)



Source: Central Bureau of Sstatistics, 2005.

5.2. Challenges for Social Security System

With regard to the developing member countries ADB (2005a) outlines (a) finding the resources to fund social protection and (b) using those resources to target the workers who face the greatest work-related risks as the toughest challenges in improving their systems of social protection. In fact, because of meager capacity to pay social security contribution, common people might not be willing to join the system if the financing mechanism is completely contributory in nature. For the people, who are below or near poverty line, opportunity cost of social security contribution, if made any under fully funded scheme, will certainly be higher than the benefits they expect from the system. While looking from the government side, it is already running in large amount of budget deficit and can barely finance additional schemes that are completely non-contributory.

Even if government aims to provide some sorts of social security in means-tested basis, as is done currently through various programs, it is quite difficult to reach to the neediest ones because of the centralized administrative structure and lack of good governance. Self-funded schemes have emerged in many countries because of their inherent nature minimizing government burden on social security and favorable impact on economic growth. But, such schemes cannot attract poorest quarter and can never cover the whole population in developing countries where large percentage of population survives in poverty. Therefore, some sort of government assistance is preferable even in the funded schemes so that it is possible to arrange certain level of redistribution that attracts greater number people in the scheme. Gillion et al（2000; 423）write that implementation of defined contribution scheme and privatization of administration will not contribute to increased coverage unless this is subsidized in some way by government. Concerning to the financing problem, a mixed effort sounds feasible.

Given the large volume of informal economy and dominance of agriculture sector in labor market, it is a difficult task to encircle whole population by the social security programs universally. In Nepalese context, finding sustainable source of financing, identifying and reaching to the neediest people, fostering income redistribution and incorporating informal sector workers are important challenges. Nevertheless, progress in poverty reduction, capacity building and human development in Nepal is virtually dependent on the expansion of basic social services. Considering these matters, government is attempting to increase the volume of spending on social sector. Therefore, if led by the strong government commitment with cooperation all quarters of society and international agencies, Nepal can gradually overcome the existing challenges and expand the coverage of social security. In Nepal, properly integrated schemes covering greater percentage of population are not only necessary to guarantee a minimum level of living means for all but also to maintain social stability and promote economic growth in the long run.

6. Summary, Conclusions and Policy Implications

6.1. Summary and Conclusions

Although formal initiation for arranging social security services started from 1930s, social security, as such, is still a relatively new concept in Nepal. Informal measures existed from the earlier time that promoted community coordination and mutual support within the targeted societies. However, along with changing socio-economic structure, informal supports are gradually disappearing whereas risk factors are rising. Consequently, wider role of social security system is increasingly realized in the country. Before the installation of multiparty democratic government in 1990, there were only two schemes of social security, namely Employees Provident Fund and Pension, confined within government sector employees. Voluntary saving scheme and cash paying allowance program for elderly and incapables came into existence in 1990s. Moreover, EPF arranged additional social security services and government strengthened the poverty targeted short-term assistive schemes. Notwithstanding the noteworthy progress in recent years, large part of population remains beyond the coverage and the system is in its infancy until the date.

Employees Provident Fund, a self-funded social security scheme, is not only the first scheme introduced in Nepal but also remains the prominent program since its inception. With only trifling importance until early 1990s, it made worthwhile progress during the last decade. Specifically, coverage was expanded to private sector employees and additional schemes were introduced. Presently, members are also protected against accident and death, and additional payment during retirement is provided from the collective fund of the members. In addition, rate of return realized by members is considerably good which however mainly comes from the incompetent financial market. EPF is also gaining managerial efficiency and seems much responsible towards members in later years. However, although the number of participants is increasing over years, coverage is very narrow and there is no significant expansion as percentage of total labor force. Similarly, neither there is any effective income redistribution mechanism nor any considerable provision exists for risk pooling. There is no option of pre-retirement withdrawal and schemes are lacking to enhance members' choices and privileges. Briefly, despite of considerable progress made in recent years, EPF still needs many efforts to become a comprehensive social security scheme in Nepal.

Citizen Investment Trust, a voluntary saving scheme, has inherent characteristics of serving higher income people in mobilizing their saving. This plan was primarily established for capital market development and has only limited number of participants by now. Nonetheless, it is gradually arranging schemes that aim to assist members in difficulty or old age. This scheme makes no sense to low income people and merits to work as a self-funded second layer program for the upper income people. Non-contributory Pension scheme exists as a retirement support covering only government employees and selected corporations. As the beneficiaries of the Pension scheme are also benefiting form the provident fund, it has created unnecessary burden to the government by arranging multiple benefit to the same people. Therefore, Pension scheme needs to be integrated with the EPF. Presently, considering the escalating burden of pension scheme, government has just started to change the scheme into the contributory type.

Third major scheme is the Allowance program for elderly and incapables and is capable to reach local as well as informal sector because of its flat coverage to defined category. High age criteria for eligibility and minimum level of benefit have jointly made the scheme affordable. Government should keep it into affordable limit and emphasize poverty targeted means-tested benefit when the administrative structure is capable. Besides the aforementioned schemes, some assistance programs are working within the purview of social security that target low-income people and usually provide in kind assistance on means-tested basis. Moreover, non-government organizations spend considerable amount targeting underprivileged communities thus deserve good prospects in arranging social security services with government coordination in future.

Thus, from service perspective, existing system centers on financial support for old age and favors government sector employees. Particularly, government sector employees are liable to benefit from all top three schemes, namely EPF, Pension and Allowance. Contradictorily, except insignificant benefit provided through some assistive schemes, most of the low-income people are beyond the social security coverage. Further, there is no considerable provision for risk pooling and income redistribution in the whole social security arrangement. Similarly, efforts are lacking to facilitate people's access in health services. In short, existing structure of social security system is in favor of those who are already in better-off situation while majority of worse-off groups are neglected.

While looking from the administrative viewpoint, there is no single institution explicitly mandated to supervise social security affairs and integration is severely lacking between the programs. This has caused unnecessary administrative burden and meager performance of the schemes. Likewise, neither there is any comprehensive act that covers all aspects of social security nor due importance has been given in policy formation. This shows lack of government efforts to extend social security for the entire population. Centralized administrative structure, frequent changes in government and alarming social conflict constitute among the hampering factors for better designation of the system. From the coverage aspect, high volume of informal labor market and dominance of agriculture-dependent self-employed population pose severe challenge for expanding social security coverage. Moreover, from the financial aspect, low contributing capacity of both government and individuals and development priority in the country make social security schemes much expensive. Nonetheless, a basic framework of social security system covering minimum services to all can certainly yield multiple benefits in Nepal where social inclusion, poverty alleviation and empowerment are major agendas for economic development. Above all, Nepal needs some fundamental reforms and additional initiatives on social security for making the system integrative, broader and sustainable. Following implications are also applicable for many other developing countries with similar institutional setting of social security system at present.

6.2. Policy Implications

Integrating schemes to avoid multiple benefits

Firstly, multiple benefits to the same group should be cut by integrating existing schemes. As the government has already decided to change the existing pension provision into contributory plan, it is more relevant to integrate the Pension scheme with the EPF on gradual basis. Initiation can be taken by encouraging government sector employees to rely only on EPF for their retirement financing by providing special incentives. Similarly, elderly allowances are not necessary to those who are receiving benefits under other scheme in their old age. So far possible, same government body should regulate all retirement related schemes that helps to minimize administrative cost in addition to avoiding multiple benefits. For promoting assistance to the poor, poverty alleviation fund is a new initiation which should be developed as an integrated plan by replacing all other temporary schemes.

Expanding coverage and incorporating health services

Secondly, it is of prime importance to enlarge coverage and incorporate health services into the system. To incorporate entire population, including agricultural and informal sector workers, government can go through two types of fundamental programs. These are: A）Expanded form of EPF and B）Social Insurance. EPF has potentiality to incorporate health sector and bring larger number of employees as well as high-income people（non-employees）into its coverage by following means. a）Extending compulsory coverage for organized private sector employees; b）Encouraging upper-income people to participate by permitting tax-exempted voluntary contribution; c）Encouraging others to join EPF voluntarily allowing flexibility in contribution rate; d）Creating members' sub accounts with EPF to better utilize their accumulated fund for arranging pre-retirement, retirement and health care benefits. However, such modification in legal provision cannot attract large percentage of population who are involved in informal and agricultural sector.

Therefore, for targeting low-income people, who are mostly rural residents, informal sector workers and agricultural workers, government can introduce social insurance scheme, as a second fundamental scheme. Insurance can be provisioned differently in different localities usually through community mobilization based on the capacity of local government, social infrastructure and other circumstances. Financing can be made by premium collection and assistance granted by the government. However, for the introduction of such scheme, a detailed study should be made regarding its management, financing mechanism and a suitable way of service delivery. As an upper layer to these two fundamental plans, voluntary saving scheme and government assistance（mainly working on means-tested basis）can be arranged for high-income and low-income people respectively.

Modifying primary social security objective

Thirdly, as the poverty is widespread and inequality is widening in the country, major objective of social security system should be on dealing with such problems. In

Nepal, social plight lies on social exclusion, lack of empowerment, widening risks and difficulty in accessing the goods of basic needs. Presently, though there is not explicit objective of social security system in Nepal, implicit priority is on old age. Therefore, while considering the country circumstances, primary focus of social security should be on meeting social risks and vulnerabilities, fostering equitable access to basic needs and enhancing redistribution of income and opportunities. Moreover, rather than simply assisting poor, focus is needed on the creation of opportunities for poor either through launching poor-targeted income generating programs or by other interventions in the labor market. There is also possibility to promote security services in rural areas, by promoting multi-sector collaboration including communities and the private sector, for upgrading living condition of lower income people by minimizing risks and enhancing their access to the goods of basic needs. After all, given the feeble administrative structure and poor financing capacity, strong government commitment and public willingness towards arranging social security services are important for making the system broad, effective and sustainable. Finally, a universal (in terms of population coverage at first) and integrative social security system can be a major vehicle for socio-economic transformation with multi-faceted contribution in Nepal.

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