Who is covered and who underreports: Access to social insurance on the Egyptian labor market

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A thorough evaluation of this new law combined with proper planning of its implementation is urgently needed. Finally, these reforms should be supported by a more rigorous enforcement of social insurance law and awareness campaigns highlighting the benefits of social insurance and its system regulations, particularly among women and youth.

References


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that exist in the metropolitan and the urban regions, relative to rural areas. It could also be due to how the urban workers value social security relative to their rural counterparts. Finally, the likelihood of underreporting increases with the worker’s monthly basic salary. In other words, low-income workers may be paying contributions on their entire wage, while high-income workers are paying contributions only on a part of their wage.

Gender and marital status do not have any significant effect on the probability of having an underreported wage to social security authority. The probability of underreporting insurable wage decreases with education level. Compared to agriculture and fishing, the probability of underreporting among private sector wage workers in higher in the transportation, storage and communication economic groups. As expected, the probability of underreporting is significantly higher for workers in smaller firm size, relative to the largest firms. Within the private sector, this probability is highest among workers of small size firms (10 or below) followed by large size firms (50 and above) and is lowest among medium size firms.

Discussion and policy recommendations
The results presented in this brief confirm several shortcomings of the Egyptian social insurance system, which have been highlighted in the literature. First, the high social insurance contribution rates, requested from both employers and employees, create a disincentive for participation. Second, the system acts as a regressive tax due to the presence of a maximum ceiling on pensionable wage. This ceiling encourages wage workers to underreport their wage to the social security authority in order to lower their contributions and avoid paying contributions on the unreported wage. When the system reaches a certain level the system loses the ability to redistribute the contributions that have been collected from the high-income group to the lower-income group. Third, the fact that pension amount is based on average monthly earning for the last five years of contributions undermines the incentive to report their pensionable wage during their first years of service and fully report their wages near the end of their service period. This community behavior is also connected with weak law enforcement, which gives room for workers and employers to get around the system in order to pay lower contributions (Helmy 2008, Siervogel and Selwaness 2012).

Prior to the January 25th, 2011 revolution, a significant reform of the social insurance system was pushed through Law 135 of 2010, during the time of the old regime in Egypt. This law was scheduled to go into effect in January 2012, but due to the event of the revolution, the status of this law is still unclear.

The essence of this new law is to remove the ceiling on pensionable wage and closely connect the worker paid contributions during his/her working years to what he/she gets as retirement pensions. This is a major change, since the earlier scheme only connected retirement payment to the last five years of contributions. This new law also highlights in the literature. First, the high social insurance contribution rates, requested from both employers and employees, create a disincentive for participation. Second, the system acts as a regressive tax due to the presence of a maximum ceiling on pensionable wage. This ceiling encourages wage workers to underreport their wage to the social security authority in order to lower their contributions and avoid paying contributions on the unreported wage. When the system reaches a certain level the system loses the ability to redistribute the contributions that have been collected from the high-income group to the lower-income group. Third, the fact that pension amount is based on average monthly earning for the last five years of contributions undermines the incentive to report their pensionable wage during their first years of service and fully report their wages near the end of their service period. This community behavior is also connected with weak law enforcement, which gives room for workers and employers to get around the system in order to pay lower contributions (Helmy 2008, Siervogel and Selwaness 2012).

Key Messages:
- Acquiring social insurance coverage in the private wage sector is more expensive than in any other sector, which reduces access to it.
- Experience has no effect on acquiring social insurance coverage among non-wage workers.
- Poor men, older, married, better educated and white collar highly skilled wage workers are more likely to have social insurance coverage.
- Linking pensions to actual paid contributions is crucial in reducing evasion.
- A major shortcoming of social insurance law combined with awareness campaigns, particularly among women and youth, is urgent needed.

Social insurance system in Egypt: long established but poorly enforced?
Egypt has a history of providing social security and social assistance programs. Following the socialist 1952 revolution, Egypt has implemented a widely stratified social insurance system (SSI) operated as a fully funded scheme where employees pay their contributions that should be invested and reaped to them in the form of old age pensions. This system has gradually shifted to be partially funded Pay-As-You-Go (PAYG) only with defined benefits (DB) schemes. Under this DB-PAYG scheme, the contributions of current active members are used to pay the pensions of the retired members, and workers who become insured in the future are no longer able to benefit from the average monthly wage increase in the last five years before retirement (ILO 2009; SSA 2011). The total monthly wage used for calculating contributions had a maximum ceiling of 1275 EGP in 2006, 1,925 EGP in 2009 and is currently 2,100 EGP (ILO 2011). The total monthly wage used for calculating contributions had a maximum ceiling of 1275 EGP in 2006, 1,925 EGP in 2009 and is currently 2,100 EGP (ILO 2011). Contributions are set as a fixed percentage of the pensionable wage or the wage reported to the social security authority up to the determined ceiling levels. The total contribution rate paid by employers on employees' pay is an average of 16.5% and decreases the employer's contribution on behalf of their employees to an average of 10%. Employees would also have the right to pay higher contributions if they want. Under this reform, the retirement age would be 65 instead of 60 years old. This increase in age is supposed to occur gradually in 2013, 2015, 2017, 2019 and 2021 and finally reaching 67 in 2027. Also, Law 135 introduced new measures to include workers in the informal economy and in activating unemployment pensions, which had been inactive in the earlier law (SSA 2011). Hence, the law of 2010 was supposed to remedy many of the shortcomings of the original social insurance system. Nevertheless, it is expected that the managing strategy of the notional accounts proposed under this new law will be a mark of either success or failure of the new social insurance system. Also, an overall reduction in the contribution rate to the Social Security system was expected to increase the contribution rate paid by employees, which would have resulted in lower contributions paid by employers. It also sheds light on the phenomenon of underreporting and its determinants of having social insurance coverage on the Egyptian labor market.

This brief identifies the worker- and enterprise- level determinants of having social insurance coverage on the Egyptian labor market. It also sheds light on the phenomenon of underreporting of the basic salary to the social security authority in the private labor market in Egypt.

In Egypt, as in many developing countries, the convergence of poverty and lack of social security places the working poor in a very vulnerable situation that mandates immediate action in research and programmatic interventions. Before the January 25th, 2011 revolution, a focus on social insurance was relevant in the view of the insurances instigated by international liberalization and the shrinking role of the state in services and employment. The revolution and its aftermath heightened social awareness and labor protests mandated a serious re-evaluation of recent labor market policies and the social protection system in Egypt. This makes issues of social security, employment and household livelihood strategies of particular importance.

The results presented in this brief confirm several shortcomings of the Egyptian social insurance system, which have been highlighted in the literature. First, the high social insurance contribution rates, requested from both employers and employees, create a disincentive for participation. Second, the system acts as a regressive tax due to the presence of a maximum ceiling on pensionable wage. This ceiling encourages wage workers to underreport their wage to the social security authority in order to lower their contributions and avoid paying contributions on the unreported wage. When the system reaches a certain level the system loses the ability to redistribute the contributions that have been collected from the high-income group to the lower-income group. Third, the fact that pension amount is based on average monthly earning for the last five years of contributions undermines the incentive to report their pensionable wage during their first years of service and fully report their wages near the end of their service period. This community behavior is also connected with weak law enforcement, which gives room for workers and employers to get around the system in order to pay lower contributions (Helmy 2008, Siervogel and Selwaness 2012).

In October 2013, the minimum wage of EGP 875 was increased.
amounts to 41% of basic wage and 25% of variable wage, which is paid by employees, employers and the government.

According to the law, participation of wage workers in the social security system is compulsory (79/1975) but voluntary for non-wage workers (law 197/1976). Nevertheless, not all private sector employers follow the law. The high social insurance contribution rates required from employers cause many of them to either underreport the basic salary of their employees to the social insurance authority or not cover their workers at all (Helmy 2008). On the other hand, some wage workers working for public sector jobs may choose not to be insured because they might minimize their opportunities of being employed in the public sector (Barosum et al. 2009). Also, wage workers may negotiate with their employers for higher pay in return for not having social insurance. Many others are quite ignorant about the whole system of social insurance and its benefits (see Sieverding 2012).

Data and methods

The results presented in this brief are based on a study on the dynamics and determinants of access to social insurance on the Egyptian labor market (see Roushdy and Selwaness 2012). Using data from two rich nationally representative labor force surveys—the 1998 Egypt Labor Market Survey (ELMS 98) and the 2006 Egypt Labor Market Panel Survey (ELMPS 06)—this study addresses two questions: Who has social insurance coverage? and who has his/her basic salary underreported? The first question investigates the worker- and enterprise-level determinants of having access to social insurance. The second question analyzes the risk of underreporting insurable wage to the social security authority. Probit regression techniques are used in these analyses.

How long it takes to get access to social insurance coverage?

Descriptive statistics show that wage workers are more likely to have social insurance compared to all types of non-wage workers, including employer, self-employed and unpaid family workers. Access to social insurance among all workers declined from around 52% in 1998 to less than 42% in 2006 (Figure 1). The observed decline in access to social insurance in 2006 has been fairly broad, cutting across both wage and non-wage workers. Nevertheless, this decline has been more prominent among employers (13 percentage points decline) and employees (7 percentage points decline) relative among wage workers (5 percentage points decline). With reference to the above, Figures 2 and 3 turn to exploring the role of job tenure in acquiring social insurance coverage.

Focusing on wage workers, Figure 2 presents the percentage distribution of first jobs for wage workers by year of entry into the labor market and sector of employment (public, private with social insurance coverage and private with no social insurance coverage), during the period 1970-2006. The share of private sector wage workers who had no access to social insurance during their first job, although growing, remains minimal. In contrast, uninsured wage employment has been making up a substantial and growing share of total first jobs since late 1980s.

The share of private sector wage workers, who had no access to social insurance coverage during their first job, reached its peak of 52% of first employment in 1999. This confirms the known fact about the failure of the private sector in Egypt, not only in absorbing all new entrants after the shrinking role of the government sector, but also in insuring formally or social security coverage to all its entrants.

Figure 2: Distribution of First Job of Wage Workers by Year of Entry and Employment Status, Working Age Population (15-64), 1960 to 2006

Who gets social insurance, and where are the jobs offering social insurance coverage found?

The multivariate analysis of the determinants of access to social insurance revealed that men and married wage workers are more likely to have social insurance coverage. The second question following the guaranteed employment scheme of the 1960s, the Egyptian public sector was the main creator of formal employment opportunities and typically the preferred sector by most new entrants to the labor market. As expected, acquiring social insurance coverage in the private sector does not often come at first entry; gaining such access takes time.

Figure 3 turns to exploring the role of job tenure in acquiring social insurance coverage. This figure compares the share of the private sector wage workers who had access to social insurance coverage, during the period 1970-2006, among those with 5 years working experience and among those with 10 years of experience. As expected, acquiring social insurance coverage in the private sector does not often come at first entry; gaining such access takes time.

The share of private sector wage workers with no social insurance is highest among labor market first entrants, followed by those having 5 years of experience, and lowest among those with at least 10 years of working experience. However, as discussed above, the percentage of those with no social insurance has been increasing over time among all the three working experience categories.

Figure 3: Distribution of Uninsured Private Sector Wage Workers by Job Tenure, Working Age Population (15-64), 1960 to 2006