Legislative Council
Panel on Welfare Services

Annual Inflation Adjustment of the Standard Payment Rates under the Comprehensive Social Security Assistance Scheme and the Social Security Allowance Scheme

PROBLEM

The standard payment rates under the Comprehensive Social Security Assistance (CSSA) Scheme and the Social Security Allowance (SSA) Scheme are adjusted every year in anticipation of the forecast inflation in the following year. The lower than expected actual inflation rates in 1997/1998 and 1998/1999 means that the combined inflation adjustments in the past two years were 6.5% higher than what was necessary to maintain the purchasing power of the standard payments. Moreover, to adhere to the forecasting methodology for adjusting these rates in a deflationary environment would mean a further reduction in the rates from 1 August 1999.

PROPOSAL

2. We propose to freeze the standard payment rates under the CSSA and SSA Schemes at their present levels until inflation in subsequent years catches up.

3. We also propose to discontinue with the current practice of adjusting standard payment rates under the CSSA and SSA Schemes according to the forecast inflation for the following year. In future, when the effects of the over-projection have been fully offset, we will consider making annual adjustments to the rates based on the actual year-on-year movement of the Social Security Assistance Index of Prices (SSAIP).[1]

JUSTIFICATION

Discrepancy between Projected and Actual Inflation

4. In the annual inflation adjustment exercise in 1998, *vide* FCR(98-99)10, we proposed and the Finance Committee (FC) agreed to increase the standard payment rates by 4.8% from 1 April 1998 in anticipation of the projected increase in SSAIP for 1998-99. We also informed FC that there had been an over-projection of SSAIP inflation rate of 1.5% in 1997-98.

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[1] We use the SSAIP rather than the Consumer Price Index (CPI) because the SSAIP measures inflation according to the expenditure pattern of CSSA recipients. The SSAIP consists of the same items as the CPI, except for those items such as rent, which are covered by “special grants” under the CSSA Scheme. The Census & Statistics Department compiles SSAIP on a monthly basis.

5. It is a well established principle that if the forecast increase in SSAIP proves to be different from the actual increase, we should take the difference in to account in calculating the adjustment for the following year. However, in order to give CSSA and SSA recipients the benefit of a full 4.8% increase in the standard payment rates, we proposed and FC agreed to defer the subsequent revision date by four months to 1 August 1999. It was then estimated that the inflation between April and July 1999 could make up for the 1.5% overshoot in 1997-98.

6. The actual movement of SSAIP for 1998-99 turned out to be -0.2%. Moreover, with a forecast negative inflation for 1999, the 1.5% over-projection in 1997-98 cannot be offset by pushing back the revision date for four months. As a result, we are now faced with a total overshoot of 6.5% (4.8%+0.2%+1.5%).

7. The Director of Audit carried out an audit investigation on the administration of the CSSA and SSA schemes from late 1998 to early 1999. During the course of the investigation, the Director of Audit noted that the combination of the over-estimation of the SSAIP and the deviations from the stated annual inflationary adjustment mechanism in the past years had a significant impact on government expenditure. He considered that the Administration should adhere to the stated annual inflation adjustment mechanism in future. He further recommended that where there were exceptional circumstances which the Administration considered that a deviation from the established adjustment mechanism was justified, the Administration should make a proposal to FC together with full relevant information.

8. If we were to follow the established mechanism for annual inflation adjustment, we would have to reduce the current CSSA and SSA standard payments by 6.5% from 1 August 1999, plus the forecast-1.3% SSAIP movement for 1999-2000, that is, a total of 7.8%.

9. We consider it undesirable to implement a 6.5% downward adjustment in the standard payment rates from 1 August 1999 because -

(a) Hong Kong has undergone a period of exceptional economic adjustment in the past 18 months or so. This has been an unsettling period for many Hong Kong citizens, especially the low income families. The 6.5% downward adjustment required will affect not only CSSA recipients but also SSA recipients who are either elderly or severely disabled people. For these people, the SSA payment may be providing a useful supplement to their household budget during this period of economic difficulties.

(b) Due to the 4.8% increase in standard payment rates in last year, the extent of downward adjustment now required is in fact larger than the actual negative inflation in 1998-1999. Some CSSA and SSA recipients, especially the elderly and disabled, may find it difficult to adapt to the 6.5% downward adjustment in the standard payment rates if it is to be implemented at one go from 1 August 1999.

10. In view of the above, we propose to maintain the standard payment rates under the CSSA and SSA Schemes at their existing levels until inflation in subsequent years catches up. We will review the year-on-year SSAIP movement on a yearly basis and consider inflation adjustments when the effects of the over-shoot have been fully offset. In this connection, we will discontinue with the current practice of adjusting the standard payment rates according to the forecast inflation for the following year. In future, when the effects of the over-adjustment have been fully offset, we will consider making adjustments to the standard payment rates based on the actual year-on-year SSAIP movement.

Inflation Adjustment in Future

11. At present, the standard payment rates of the CSSA and SSA schemes are adjusted annually in anticipation of the forecast movement of the SSAIP in the following year. The original intention was to adjust the standard payment rates in advance to maintain the purchasing power of the social security payments. However, as circumstances do change, sometimes rather abruptly, any forecast on the future, no matter how thorough and sophisticated, by its nature is liable to discrepancy against the actual outturn[2]. The discrepancies between the forecast and the actual SSAIP movements from 1989-90 onwards are shown in **Enclosure 1.**

12. The current forecast inflation methodology applied to the CSSA and SSA schemes is in fact an exception rather than rule. For the purpose of maintaining the purchasing power of financial assistance or remuneration provide by Government, the established practice is to adjust the rates in accordance with the actual movement of the relevant price index. This is the case in the adjustments to Legislative Council and District Board members' honouraria, student financial assistance, subsidy for kindergarten, etc.

13. The current forecast inflation methodology for adjusting social security payments was adopted in 1989 at a time when the standard payment rates under the social security schemes were low. Over the years, Government has made considerable improvements to the level of assistance. For example, the standard rate for an able-bodied single adult was $620 in 1989 and is now $1,805. This represents an increase of 191% as compared to inflation over the period of only 117%. Even more significant improvements have been made in respect of the standard rates for

[2] SSAIP forecast is basically derived from a time series model, namely the Auto-Regressive Integrated Moving Average (ARIMA) model, developed by the Census and Statistics Department in collaboration with the Economic Analysis Division. The ARIMA model, which is formula-based rather than judgement-constituted, is a commonly used projection technique for time series analyses in other economies overseas. However, the sharp moderation in inflation in Hong Kong observed since the early part of 1998, in line with the economic adjustment upon the impact of the regional financial turmoil, and in contrast to the higher inflation observed in the earlier years, has magnified the forecast discrepancy. Under such abrupt circumstances, it would be too demanding of such a model to produce a forecast which is deemed likely to come close to the subsequent actual outturn.

CSSA elderly and child recipients. It is therefore arguable whether it is necessary to adjust the standard payment rates in advance according to forecast inflation for the coming year.

14. In addition, the forecast inflation methodology was justified at times of high inflation. This was the case in 1989 and well into the early 1990s. But consumer price inflation has distinctly eased in 1998 and turned negative this year. It should be noted that for the purpose of Medium Range Forecast, the assumed year on year inflation has been moderated to 3%.

15. The proposed change in the inflation adjustment mechanism will avoid the problems due to discrepancies between the forecast and actual inflation. The total CSSA and SSA spending ($20.4 billion in 1999-2000) now accounts for 11.4% of total Government recurrent expenditure. About S16 billion is accounted for by standard rate payments. Hence, for every 1% of over-estimate that could not be made up for would mean that Government had to unjustifiably spend $161 million a year. This amount, if ploughed back to direct services, would provide 1 700 residential care and attention places for the elderly or 2 100 day care centre places for the elderly.

FINANCIAL IMPLICATIONS

16. A6.5% reduction in standard rates from 1 August 1999 would result in reduced Government expenditure of $707 million in 1999-2000 ($1,062 million in a full year). The proposed freeze would mean that we would need to incur this amount that could otherwise be saved and go some way towards relieving the spending pressure of CSSA/SSA. On the other hand, if the money were diverted to provide direct services, it would provide over 11 000 residential care and attention places for the elderly or over 13 000 day care places for the elderly. The actual amount of savings foregone in any subsequent year will depend on the inflation rate in that year. A further breakdown of the financial implications for 1999/2000 is as follows:

		$ million
(a)	not implementing the 6.5% downward adjustment in CSSA standard payment rates	**497**
(b)	not implementing the 6.5% downward adjustment in SSA standard payment rates	**210**
	Total	**707**

17. The rapid growth in social security expenditure in recent years, particularly CSSA, remains a concern of the community. CSSA expenditure has increased from $2.4 billion in 1993-94 to $13 billion in 1998-99 (representing an average increase of 31% in real terms every year). It is projected to rise to $15.5 billion in 1999-2000,

which is 8.6% of total Government recurrent expenditure. The current proposal not to bring down the rates to reflect the over-projection on compassionate grounds and its consequential impact on CSSA/SSA expenditure in the following years until inflation catches up will create added pressure in this area of spending.

18. In view of the current economic downturn and rising unemployment, CSSA will continue to perform its safety net function to support those in need. However, we have to look at all aspects of CSSA Scheme and its administration to ensure equity in the use of limited public resources. The Social Welfare Department has started to implement a Support for Self-reliance Scheme in June 1999. The aim is to encourage and assist those CSSA recipients who are able to work to actively seek work and become self-reliant. The Department will also step up fraud prevention efforts to ensure that financial assistance is targeted at those genuinely in need. We will need to sustain our efforts in these and other areas concerning the CSSA Scheme.

BACKGROUND INFORMATION

19. The social security system administered by the Social Welfare Department comprises two schemes: the CSSA Scheme and the SSA Scheme. An explanatory note is at **Enclosure 2.**

Health and Welfare Bureau
June 1999

Enclosure 1

Annual inflation adjustment for CSSA and SSA Standard payment rates

Financial Year	SSAIP forecast increase for the year (A)	Adjustment to account for over-projection under-projection in the previous year (B)	Increase in standard payment rates approved by FC (C)=(A)+(B)	Actual SSAIP movement for the year (D)	Actual SSAIP movement vis-a-vis forecast (under-projection in negative) (E)=(A)-(D)
1989-90	8%	+3%	11%	9.8%	-1.8%
1990-91	8%+1.8%	10%*	8.1%	-0.1%	
1991-92	9%	0	9%	10.3%	-1.3%
1992-93	9.5%	+1.3%	10.74%*	8.3%	1.2%
1993-94	9%	0	9%	7.7%	1.3%
1994-95	7.7%	0	7.7%	7.1%	0.6%
1995-96	8.5%	0	8.5%	6.2%	2.3%
1996-97	7%	0	7%	3.4%	3.6%
1997-98	6.5%	0	6.5%	5%	1.5%
1998-99	4.8%	The 1.5% over-projection in the previous year to be off-set by deferring the next adjustment date for four months	4.8%	-0.2%	5.0%

*These are due to rounding effect of the rate increase.

Enclosure 2

Social Security System

Introduction

The social security system provides a safety net for individuals or families suffering financial hardship for various reasons, such as old age, disability, illness, unemployment, low earnings, etc. The aim of the Comprehensive Social Security Assistance (CSSA) Scheme is to assist such individuals or families in meeting basic and essential needs of livelihood. The aim of the Social Security Allowance (SSA) Scheme is to help the severely disabled and the elderly to meet the special needs arising from disability or old age. A person can receive either assistance under the CSSA Scheme or one of the allowances under the SSA Scheme.

Eligibility

2. Both schemes are non-contributory. The CSSA Scheme is means-tested. Applicants for SSA are not subject to means test except that persons aged between 65 and 69 applying for the Old Age Allowance have to declare that their income and assets do not exceed the prescribed levels.

3. There are residence requirements for both Schemes. In addition, applicants for CSSA aged between 15 and 59, if unemployed and in normal health, are expected to seek work actively and report their employment condition to staff of the Social Welfare Department regularly with effect from 1 June 1999.

4. Starting from 1 April 1997, elderly persons aged 60 or above, who have been in receipt of CSSA continuously for three years, may join the Portable CSSA Scheme whereby they are allowed to continue to receive their monthly standard payments and annual long-term supplement should they choose to retire permanently in Guangdong.

Comprehensive Social Security Assistance Scheme

5. The amount of assistance is determined by the resources and needs of the applicant. The difference between the applicant’s income and his total recognized needs as determined by reference to certain prescribed levels, will be the amount of assistance payable.

6. The Scheme embraces different standard payments to meet the basic and essential needs of broad categories of recipients. In addition, starting from 1 June 1999, an annual long-term supplement is payable only to those elderly, disabled and ill-health recipients who have been receiving assistance continuously for more than 12 months for the replacement of household and durable goods. A monthly supplement is also paid to single parents in recognition of the special difficulties they face in bringing up families on their own without the support of spouses. Apart from these standard payments, a wide range of special grants are payable to meet the specific needs of an individual or family. They include payments to cover such expenses as rent, water charges, school fees, child care centre fees and burial grants.

Social Security Allowance Scheme

7. Four allowances are payable under this scheme as follows -

(a) Normal Disability Allowance

For severely disabled persons who, broadly speaking, suffer from a 100% loss of earning capacity, or who are profoundly deaf.

(b) Higher Disability Allowance

For severely disabled persons who require constant attendance from others in their daily life but are not receiving such care in a government or subvented institution or a medical institution under the Hospital Authority.

(c) Normal Old Age Allowance

For persons aged between 65 and 69 whose income and assets do not exceed the prescribed levels.

(d) Higher Old Age Allowance

For persons aged 70 or above.