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The Social Security System in Sri Lanka

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Abstract: **Laws pertaining to social security exists to provide social benefits to both public and private sector employees through pension funds and other similar means. Benefits incurred to individual employees through such funds and its ablity to address social issues faced by employees post- retirement and in the course of employment, ought to be investigated into in order to identify the degree of protection law provides to such employees. A strong social security system is the reflection of a true democracy that strives to fullfill its obligation to its people by mandating individual contribution.**

***Keywords*: Society, Security, Employees, Constitution.**

1. INTRODUCTION

The system of social security is widely believed to have been instituted after the Great Depression in America[1] with the enactment of the Social Security Act of 1935 as part of the recovery series. The idea of social security, however, is much older and dates back to 1797 when it was first proposed by Thomas Paine. In his pamphlet titled 'Agrarian Justice', Paine proposed the creation of a social insurance scheme that would provide for the elderly and disabled as well as the young just starting out in life[2], to be paid from an accrued national fund financed by a tax imposed on landowners. Even though the scheme suggested by Paine was built on an antiquated approach, it rooted the need for the creation of a national fund to provide income security for the elderly and the vulnerable.

The universal need for social security is now recognised by the global community as a human right. It has been enshrined in Articles 22[3] and 25[4] of the Universal Declaration of Human Rights and Article 9[5] of the International Covenant on Economic, Social and Cultural Rights. It has also been a core mandate of the International Labour Organisation (ILO) since its inception in 1919, in order to realize which, several international conventions have been set out. These conventions include, inter alia, Social Security (Minimum Standards) Convention No. 102; Maternity Protection Convention No. 103; Invalidity, Employment Injury Benefits

[1] An economic slump in North America, Europe, and other industrialized areas of the world that began in 1929 and lasted for about a decade.

[2] Conley, B. *'Social Security was first proposed by Thomas Paine'* <http://brendanconley.com/social-security-was-first-proposed-by-thomas-paine/> accessed 06 November 2015

[3] Everyone, as a member of society, has the right to social security and is entitled to realization, through national effort and international co-operation and in accordance with the organization and resources of each State, of the economic, social and cultural rights indispensable for his dignity and the free development of his personality.

[4] (1) Everyone has the right to a standard of living adequate for the health and well-being of himself and of his family, including food, clothing, and housing and medical care and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood in circumstances beyond his control.

(2) Motherhood and childhood are entitled to special care and assistance. All children, whether born in or out of wedlock, shall enjoy the same social protection.

[5] The States Parties to the present Covenant recognize the right of everyone to social security, including social insurance.

2. LITERATURE REVIEW

Convention No. 121 and Old-Age and Survivors' Benefits Convention (No. 128). Among the Conventions pertaining to social security, Convention No. 102 remains of utmost importance as it is the flagship of the eight up-to-date social security Conventions[6]. It is the only international Convention which encompasses the nine classical branches of social security and sets minimum standards for each. These are: medical care, sickness benefit, unemployment benefit, old-age benefit, employment injury benefit, family benefit, maternity benefit, invalidity benefit and survivors' benefit.

While the Constitution of Sri Lanka does not directly provide for social security, Articles 27(2)[7] and 27(9)[8] of the same affirms the responsibility of the state to provide for basic standards of living and to ensure social security and welfare respectively. Of ILO's conventions concerning social security, although Sri Lanka has thus far only ratified the Maternity Protection Convention No. 103, it is important to note that various provisions have been in existence domestically to grant social security even before the ILO was established in 1919. The crown being the model employer, considered that adequate provision should be made to its employees in their retirement[9] and consequently brought into effect a mandatory pension scheme for civil servants in 1901. The Medical Wants Ordinance of 1912 and the Diseases (Labourers) Ordinance of 1912 recognized the need to provide medical care to employees about four decades prior to the adoption of the Convention No. 102 in 1952, which was ILO's first and foremost convention to have secured employees' entitlement to medical care.

The current social security system of Sri Lanka:

At present, the social security system of Sri Lanka does not specifically provide a social insurance scheme as Convention No. 102 demands. The reason being, most of them take the form of provident funds or retirement savings schemes and exist both in the formal and informal economy, yet covers only about 22% of the population above the age of 15[10] whereas Convention No. 102 requires at least 50% of the population to be covered.

The Public Servants' Pension Scheme (PSPS), Public Servants' Provident Fund and Widows' and Orphans' Pension (W&OP) administered by the Department of Pensions of Sri Lanka, cover the public sector employees and their families. The PSPS is a 'defined benefit' scheme in which, the monthly benefit is calculated as a percentage of the salary and in proportion to the individual's number of years of service in the public sector. It is financed by the government budget and entitles members to an old-age pension subsequent to ten years of service in a permanent post and is payable from age 50 for women or 55 for men. In *Ranasinghe v Attorney General*[11], the court recognized the plaintiff's right to a pension for a period of 13 years for which he was not issued a formal confirmation letter following his probationary period. Further, in the case of *Premathillake v Withanarachchi and others*[12] the court held that the pension should be calculated based on the salary drawn as at the plaintiff's date of retirement taking into account any salary increment even if such increment was granted on the very same day of retirement. The W&OP established under Act No. 24 of 1983 entitles dependents of the late pensioner, i.e. spouse, children (until the age of 22) and disabled children (during their entire lifetime) the assistance to which the late pensioner was entitled at the time of his/her death, in its full amount for the spouse and in a portion of 50% for the children.

While public sector employees are protected in their old-age by schemes discussed above, there are statutory provisions such as the Employees' Provident Fund (EPF), Employees' Trust Fund (ETF) and Gratuity to provide for employees in the private sector.

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[6] Hempel, F., Gulibault, E. & Kulke, U. *'Social Security (Minimum Standards) Convention No. 102 (1952)'* < http://www.social-protection.org/gimi/gess/ShowTheme.do?tid=722> accessed 08 November 2015

[7] The State is pledged to establish in Sri Lanka a democratic socialist society, the objectives of which include –
(b) the promotion of the welfare of the People by securing and protecting as effectively as it may, a social order in which justice (social, economic and political) shall guide all the institutions of the national life ;

[8] The State shall ensure social security and welfare.

[9] Rajalingam, R. '*Employees Provident Fund'* in *Understanding Labour Law* (2nd edn Colombo 2001)

[10] *'Social Security in Sri Lanka'* <http://www.social-protection.org/gimi/gess/RessourcePDF.action; jsessionid=42be4011a5ee152caddde4737ae20648ebd69e086d44b8b1de3338d7c63d5f03.e3aTbhuLbNmSe34MchaRahaKb3z0?ressource.ressourceId=7055> accessed 14 November 2015

[11] (1981) 2 SLR 453

[12] (1998) 3 SLR 221

– The EPF established under Act No. 15 of 1958 remains the most significant old-age benefit scheme with an important effect on the economy of the country. Individual accounts are activated for all private sector employees where both the employer and the employee contribute at a respective rate of 12% and 8% of the employee's monthly wage. The scheme essentially provides relief in the form of the accumulated lump sum along with the interest, during old-age, disability and survivorship. The interest is annually determined by the monetary board and is fixed at a rate not less than 2.5%. Old-age benefits are payable upon retirement (55 for men and 50 for women) or at an instance when the receiver migrates permanently, while disability benefits are granted following the assessment of incapacity to work. In the case of *Ratnaweera v Goonethilleke*[13], the court held that the employer was liable to contribute to the fund for the month even though the employee did not work for the full month.

– Initiated in 1981 to encourage ownership of shares among employees, the ETF is also a defined contribution scheme established under Act No. 46 on 1980. The fund is financed by contributions of 3% per cent of gross wages. Membership is also open to self-employed persons on a voluntary basis. In the unreported case of *Amarasena v ETF Board*[14] Grero J held that, an employer who fails to make appropriate contributions, whether as a person or a body of persons forming a company, contravenes the provisions of the Act and will be accountable for the omission.

– The Payment of Gratuity Act No. 12 of 1983 entitles workers whose period of service is not less than 5 years, to a gratuity. According to the Act, half the amount of the last drawn salary is multiplied by the number of years of service and is granted at the termination of services. Even though the payment of gratuity is based on a statutory provision, it must be noted that the Labour Tribunals have taken a rather flexible approach in awarding such. The case of *River Valleys Development Board v Ranasinghe*[15] illustrates that, gratuity can be calculated by a Labour Tribunal at its discretion and award a higher payment as gratuity apart from the amount that is 'legally due' as per the provisions of the Act. The Labour Tribunal has constantly acted on its responsibility to make a just and equitable order in addition to granting mere statutory relief. In the case of *Bata Shoe Company v Fernando*[16] it was held that, gratuity is payable even upon resignation by the employee, and not necessarily on termination by the employer alone as it is paid for an employee's long and meritorious services to his/her employer.

– Currently, Sri Lanka has no prescribed unemployment benefit scheme as Convention No. 102 requires. However, the Termination of Employment of Workmen Act (TEWA)[17] governs the law concerning termination of employment under particular circumstances, especially due to closure of businesses. Private sector employees who have completed a minimal service period of 6 months are eligible to be compensated by means of a mandatory severance payment made as a lump sum to the qualifying terminated workers. The minimum severance payment which was previously decided upon the discretion of the Commissioner of Labour, is now specified in the Schedule of the Act thus allowing for an increased level certainty pertaining compensation received during termination of employment arising from identified reasons.

In developing countries, the informal sector contributes much to a country's economy by producing goods and services for non-formal markets, and for people employed in the formal economy.[18] Hence, it is crucial to ensure that the informal sector is adequately protected. A major deficiency in Convention No. 102, which suggests that ratification of the same will not substantially alter the social security system of Sri Lanka, is that the Convention only covers a certain percentage of the population comprised of those in the formal sector, while it fails to reflect the needs of the majority which is made up of employees in informal economy. However, based on the socio-economic landscape of the country, recognizing the need to protect the informal sector, three schemes operate in Sri Lanka for this purpose, namely: the Farmers' Pension Scheme established under Act No. 12 of 1987, Fishermen's Pension and Social Security Benefit Scheme established under Act No. 23 of 1990 and Pension and Social Security Benefit Scheme for the Self-employed established by the Social Security Board Act No. 17 of 1996. These are voluntary pension schemes and are open for those between the ages of 18 – 59. It is predominantly funded by contributions made by the members themselves in a percentage that differs based on the age at which the contributor enrols. Upon attaining the age of 60, the contributor is entitled to a monthly pension. In cases of

[13] 65 NLR 89
[14] CA Application No. 1186/90
[15] (1986) I CALR 92
[16] (1986) 2 CALR 233
[17] No. 20 of 2008
[18] Sanderatne, N. '*Exploring the Complexity of the Informal Economy*' <http://www.sundaytimes.lk/140406/business-times/exploring-the-complexity-of-the-informal-economy-91223.html> accessed 19 November 2015

permanent/partial disability, the contributor is entitled to a monthly allowance or the accumulated lump sum inclusive of the interest, while at the event of death of contributor the spouse is entitled to a death gratuity.

Drawbacks of the existing system:

Among south Asian counties, Sri Lanka has achieved the highest level of social security thus far with multiple schemes covering different classes of employees. However, globally this level remains insufficient as the existing schemes fail to offer ample protection under all nine limbs of social security addressed in Convention No. 102. The system lacks schemes that individually provide protection for separate branches which result in a single scheme being made available to offer for protection under many limbs, thereby resulting in the relevant scheme not being able to provide complete protection under at least one limb. For example, the EPF Act was amended in 2012 inserting S.23A providing that every member of the fund who has made contributions for a minimum period of 10 years and possessing a minimum amount of Rs. 300,000/- will be entitled to withdraw 30% of the fund for the purposes of housing and medical treatment prior to attaining the stipulated age to be entitled to the EPF payments. Further, in both EPF and ETF up to 75% of the member's contribution is allowed to stand as a security against housing loans. While it is true that the flexibility thus offered is nevertheless to ensure a form of social security by providing for housing and medical care, such provisions also reflect that the main objective of the scheme in providing old-age benefits does not fully realize as a significant proportion of the funds get exhausted prior to the contributor reaching old-age. In case of loans obtained against the funds, the complication arises when members fail to reimburse the loan with interest, thus being left indebted and the accumulated funds being deducted against the obtained loan, again leaving insufficient funds to provide protection during old-age, illness or invalidity.

Apart from the public sector employees covered by the PSPS, the rest of the schemes available for employees in the formal sector deliver benefits in the form of a lump sum and not as fixed periodical payments. As a result of this, at the time of reaching the specified age to be entitled to withdrawing the EPF and ETF funds, the member is placed in a position that requires him/her to manage the lump sum benefit in a way that would provide an income on a monthly basis. At the event of failure to invest in such a manner, the members are mostly found having spent the withdrawn funds on other purposes. Gratuity, being awarded soon after termination, becomes less favourable in providing social security during old-age as there is no obligation to at least transfer a part of it to the individual's EPF in order to be utilized during old-age. Hence, as with the payment of gratuity obtained, an identical situation arises whereby these funds too are used in mostly fulfilling immediate temporary needs instead of saving for long term benefits.

Lack of coordination between schemes in terms of management and financing effects the efficiency of the social security system in providing adequate return and results in the duplication of the same functions. Various schemes that exist for a common purpose being administered by different ministries and departments tend to multiply administrative costs and in turn lowers the rate of return to individual members. Weak co-ordination complicates the process of individual funding and causes inconvenience when claiming the accumulation as the same individual is required to go through several clerical procedures to claim from different funds existing for the same purpose. When the Hon. Prime Minister recently proposed for the merging of EPF and ETF to set up a new pension scheme for private sector employees, a collective objection was encountered when the Ceylon Bank Employees' Union fired a salvo against the government plan.[19] The objection was made owing to the reason that the said proposal suggested to remove the control of the Central Bank and the Ministry of Labour Relations over the said funds which could potentially subject the merged fund to the threat of being entirely invested in the share market, whereas at present it is predominantly invested in government securities such as treasury bonds and bills. A major drawback of the existing decentralised system is the lack of supervision with regard to investments and its corresponding performance, which thereby result in a lower return on investment. Due to the lack of legal obligations in subjecting the funds to a regular actuarial review, at present there is barely a proper evaluation of the viability of funds. If the state, in allowing the EPF-ETF merger to be administered by the Public Wealth Trust, could ensure responsible investments and safe returns along with the compulsion to perform better, the proposed fusion would better replace the existing system by bringing home higher incentives.

As with employees of the informal sector, even though funds exist to provide social security as discussed in an earlier paragraph, the mere existence does not reflect its feasibility in delivering benefits. Unlike in the case of formal sector employees whose contributions are deducted from the salary itself; for farmers, fishermen and self-employed individuals, contributing to such a fund is simply a personal obligation from which they often evade. While such evasion could also be

[19] Sri Lanka bank unions oppose EPF and ETF merger <http://www.sundaytimes.lk/151122/business-times/sri-lanka-bank-unions-oppose-epf-and-etf-merger-172061.html> accessed 22 November 2010

a result of the unawareness of the existence of such funds, it is mostly due to not having understood the importance of income security during old-age and illness. The state is, therefore responsible to create sufficient awareness and impose a legal obligation to contribute in order to provide better social security to this important yet often neglected class of employees. It is vital to note that, even though mechanisms can be set up to regularise contributions by the members, the difficulty lies in imposing such legal obligations upon individuals like the majority of fishermen who earn for the day and face severe difficulties in handling their day-to-day expenses. Providing social security to such a class of individuals becomes crucial as their livelihood it renders their position vulnerable involving the assumption of extreme physical risks in order to earn for survival. Recognizing the inadequacy of the existing social security system in providing for such individuals, the Hon. Finance Minister, in the budget for fiscal year 2016, proposed a life insurance cover of Rs. 1 million for fishermen to counter disasters taking place while fishing.[20] The scheme is also targeted to cover the expenses incurred in the search and rescue operations.

Ratification of Minimum Standards as per Convention No. 102:

To ratify the said Convention, a nation must have in operation three out of the nine branches the Convention specifies, with at least one being unemployment, old-age, invalidity or survivorship benefits.[21] Based on the different schemes established that are already in existence as discussed above, even though Sri Lanka would be eligible to ratify the said Convention with slight changes in the existing provisions, it is vital to first to recognise if ratification of such a Convention would result in an enhancement of the overall system together with a forward economic leap in a developing country like ours'. The level of benefits expected to be granted to employees remain extremely high for a tax financed universal schemes, which, developing countries like Sri Lanka cannot provide before attaining better fiscal stability. Providing beyond the country's capacity would only cause economic volatility which would decline the situation of the existing system. The Convention has also failed to address basic needs of workers in developing countries such as sanitation, minimum nutrition and minimum education for the children of employees. More importantly, as already mentioned in an earlier paragraph, the Convention does not provide for the majority of the population of Sri Lanka comprised of workers in the informal economy. Mere ratification of Convention No. 102 due to having met the minimum standards under three limbs, though might seem prestigious, would not profoundly enhance the overall social security system of Sri Lanka unless the country focuses on improving it in ways that best compliment the country's existing infrastructure, perhaps by establishing modern micro-insurance schemes or upgrading the existing ones that would work better for smaller communities. The problems

with the existing insurance schemes is that they are administered by private companies with purely profit seeking motives and they work on a competitive environment, not to provide better security for customers, rather to generate better income for the company. Undoubtedly, even though private insurance schemes have proven worth investing on, the state's intervention with the purpose of not only generating income but also to provide better social security could largely contribute to those who are in serious need of such protection.

3. CONCLUSION

Since social security systems are based on mass-scale funding, reforms require parallel improvements in the country's labour markets, financial markets and fiscal management, and thereby come into fruition only through systematic, long-term and abuse-free mechanisms. The possibility of preserving the social security system at a constant level becomes challenging to a state as minor deviations in other factors such as life-expectancy, administrative costs and even taxation could have a disparate impact on the overall system, thus resulting in an inability to achieve its goals to the same extent at all times. Apart from what the state could effectuate in order to ensure social security – which it largely has and is constantly attempting to improve – it has often been the case that, the need for social security has not been understood by many as crucial despite its importance for a dignified and independent survival. Though the cruelty of poverty is seen as a major reason why countries like ours' still remain in the developing phase, the mere observation has not led enough individuals to believe in investing on a social security system that could provide at times of adversity. A strong social security system is not merely an obligation of the state to its people: it is also a yardstick of the state's success, for which, not only the government but also every individual citizen must wilfully contribute simultaneously.

[20] Sri Lanka Broadcasting Corporation <http://www.slbc.lk/index.php/en/tamil-news-update/2546-the-new-government%E2%80%99s-first-full-year-budget,-for-the-fiscal-year-of-2016,-was-presented-to-the-parliament-of-sri-lanka-by-finance-minister-ravi-karunanayake-yesterday.html> accessed 04 December 2015

[21] Myres, R. *'Minimum Standards of Social Security: New International Convention'* <https://www.ssa.gov/policy/docs/ssb/v15n10/v15n10p3.pdf> accessed 19 November 2015

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[15] Employees' Trust Fund Act No. 46 on 1980

[16] Farmers Pension and Social Security Benefit Scheme Act No. 12 of 1987

[17] Fishermen's Pension and Social Security Act No. 23 of 1990

[18] Medical Wants Ordinance No. 9 of 1912

[19] Payment of Gratuity Act No. 12 on 1983

[20] Social Security (Minimum Standards) Convention 1952 (No. 102)

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[22] Termination of Employment of Workmen Act No. 20 of 2008

[23] Widows' and Orphans' Pension Act no. 24 of 1983

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[25] Bata Shoe Company v Fernando (1986) 2 CALR 233

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[27] Ranasinghe v Attorney General (1981) 2 SLR 453

[28] Ratnaweera v Goonethilleke 65 NLR 89

[29] River Valleys Development Board v Ranasinghe (1986) I CALR 92