Social protection in Europe 1997

Social security & social integration

Employment & social affairs

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Foreword

Social protection systems continue to provide the bulk of expenditure on social support, health care and pensions in the Member States of the EU and to play a fundamental role in ensuring income redistribution and social cohesion. They also help to maintain political stability and economic progress in the lives of citizens of the Union.

As pointed out in the Commission Communication on *Modernising and Improving Social Protection* (March 1997) EU expenditure on social protection — currently running at an average of 28.5% of GDP — should be seen not as a financial burden but rather as an investment in human resources and as a form of insurance which provides the security necessary to the successful functioning of increasingly flexible labour markets. Social protection is a productive factor which contributes to economic growth and performance. Getting this political message across will be especially important as the EU enlarges in the next few years.

However, all Member States are having to face up to the inexorable need to reform their social protection systems. As demand has risen, so at the same time financial constraints have tightened. Many of the old assumptions on which social protection systems have been built — a low level of unemployment, one full time job without any major spells of inactivity, the man as the bread-winner and so on — are disappearing. We only have to look about us to see that this world has moved on and we must move with it. Social protection systems face new challenges as a direct result of demographic change and the massive rise and persistence of long-term unemployment in our economies. Reform is an issue that cannot be ducked.

This is our third report on social protection in Europe. As in the previous two reports, we are continuing to monitor how Member States are meeting the new realities which are replacing the old assumptions. The 1993 report was a first signal of the seriousness with which these issues were beginning to be felt by Member States. In 1995 the debate sharpened with the emergence of the Commission's *Framework for Debate on the Future of Social Protection*. This third report has been produced at a time when Member States are turning a political corner on employment policy. The Treaty of Amsterdam and the special Jobs Summit that followed in November 1997 revealed the determination of EU governments to abandon the policies followed for more than three decades in favour of active labour market policies that emphasise employability, business opportunity, equality at work and, above all, a readiness to invest in the EU's most precious commodity: the skills of its people. Of all the components of the new European employment strategy, social protection is one of the most important. From the start it was understood that our social protection systems had to become more 'employment-friendly'. This report analyses what this means in practice.

The report examines the changes to the scale, pattern, growth and funding of social expenditure. It describes how social expenditure remains one of the major weapons in the fight against poverty and exclusion even while social protection systems are adapted better to fit the needs of the modern labour market. Most important of all, it logs the major policy developments in social protection taking place as more emphasis is placed on the incentive to work, as we seek to make the European work force more employable and more adaptable, as competitive pressures on businesses increase and as people in Europe get older. The policy issues associated with this process are many and complex. They range from how people qualify for benefit to how jobs are created, from how we perceive retirement to how our health systems are funded.

Above all, the report explains why these issues matter so much and why it is vital that we keep a constant eye on what is happening in this most fundamental aspect of how we organise our societies.

Pádraig Flynn

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Executive summary

The political context

This is the third report on Social Protection in Europe. It sets out to monitor the progress achieved in relation to the objectives contained in the Council's Recommendation on the *convergence of social protection objectives and policies* of July 1992 (92/442/EEC) and to update the analysis of the 1993 and 1995 reports.

The Report is also intended to contribute to the debate on the future of social protection in the Union, launched by the Commission in 1995 with its Communication *Framework for Debate on the Future of Social Protection.* In March 1997, the Commission published a further Communication, *Modernising and Improving Social Protection*, which reflected the main points made in the debate and drew attention to the major implications for policy.

The report should also be seen in the context both of Member States' efforts to consolidate public finances — as pointed out in the 1997 Broad Economic Guidelines and the two Resolutions on macro-economic stability, growth and employment, adopted at the European Council in Amsterdam — and of the European Employment Strategy. At the Luxembourg Jobs Summit in November 1997, Member States broadly endorsed the Commission's proposals for employment guidelines. They agreed that benefit as well as training systems should, where necessary, be reviewed and adapted to ensure that they actively support employability. Social protection also has an important role to play in helping to achieve other aims emphasised in the 1998 Employment Guidelines which were subsequently adopted — developing entrepreneurship, encouraging adaptability of businesses and their employees and strengthening the policies for equal opportunities. A clear link has, therefore, been established at the highest level between social protection systems and the European Employment Strategy.

The main quantitative findings

The main points to emerge from the analysis of the revised ESSPROS database on social protection and the new European Community Household Panel are:

The scale of social expenditure: expenditure on social protection in the Union amounted to $28\frac{1}{2}\%$ of GDP in 1995. This figure, however, ranged from 20% of GDP in Ireland and 21–22% in Greece, Spain and Portugal to over 30% in France, the Netherlands and the three Nordic countries, with Sweden having the highest level at almost 36%.

The pattern of social expenditure: old-age pensions are by some way the largest item of social protection expenditure in the Union, accounting for $42\frac{1}{2}\%$ of the total in 1995, equivalent to 12% of GDP, followed by health care, amounting to around 22% of the total in the Union, as well as in all Member States, except for Denmark (only 14%), and to some 6% of GDP. Transfers to the unemployed accounted for only 8% of total expenditure in the Union (just under $2\frac{1}{2}\%$ of GDP).

The growth of social expenditure: in most Member States, the increase in social protection expenditure has slowed down in recent years. Although social expenditure across the Union increased in relation to GDP between 1990 and 1995 (by just over 2 percentage points), this partly reflects the slowdown in GDP growth during the recession years. Between 1993 and 1995, spending grew no faster than GDP and in most countries rose by less.

Sources of finance: around 65% of the funding for social protection in the Union comes from social charges levied on employers and the people protected, most of the rest from general taxation. Employers' contributions alone accounted for some 40% of total finance in 1995.

Levels of unemployment benefit: a significant proportion of people unemployed in a number of Member States, according to the ECHP, received no unemployment benefit at all in 1993, even when out of work for three months or more. For those receiving benefit, the monthly amount averaged just over half of their net earnings for the months when they were working, though it ranged from 60–65% in Denmark, France and Ireland to only 25% in Greece and the UK.

The relief of poverty: social transfers (including private pensions, but excluding benefits in kind, such as health care) accounted for around 30% of net household income in the Union in 1993. For some 35% of households, they were the main source of income and without them just under 40% of households would have had a level of income of under half the national average (the conventional measure of poverty). After transfers, around 17% of households in the Union had a level of income below this.

Recent changes in policy

The economic and social context in which European social protection systems operate has changed considerably over the past decade or two (as analysed in the Commission Communication *Modernising and Improving Social Protection*). Over the 1990s, low economic growth has increased both the difficulties of funding social protection across the Union and, in combination with demographic and social trends, the number of people being supported. While income maintenance and prevention of social exclusion continue to be fundamental objectives of social protection systems, the aim of policy is to strengthen incentives to work and to improve the employability and adaptability of the work force. The major policy developments are:

Tightening of eligibility for benefit: in many Member States, qualifying conditions for benefit have been tightened and the contribution record required for eligibility has been lengthened.

Strengthening incentives to work: in several countries, measures have been introduced to try to ensure that income from work is always higher than from benefits through tax concessions for low-paid workers and in-work benefits as well as by reducing benefit rates.

Shifting towards more active policies: there is general recognition that providing income support alone is not sufficient to tackle problems of unemployment and social exclusion. In the 1998 Employment Guidelines agreed by the Council, Member States have committed themselves to bringing about a shift from passive to active measures aimed at increasing the employability of those out of work and helping them find a job.

Extending job creation schemes: in a number of Member States, job creation has been encouraged by selective reductions in social contributions as well as by direct subsidies. Member States, moreover, have agreed in the Employment Guidelines to investigate possible means of developing local employment opportunities in the social economy and new activities where needs are not being met by the market.

Reducing dependency and social exclusion: throughout the Union, social assistance guarantees a minimum level of income. The general tendency within Member States' social assistance schemes is to address underlying causes of poverty and social exclusion, to reduce reliance on benefits and to encourage all those able to work to find employment.

Helping people with disabilities: efforts have been made in many Member States to improve the employment opportunities of those with disabilities, through deterring discrimination and removing obstacles to them working, while at the same tightening eligibility for benefit.

Reversing the trend towards early retirement: there has been a long-term trend towards early retirement across the Union, pushing up social expenditure and depriving the economy prematurely of the skills which the people concerned have to offer. For women, this trend has been offset by a more powerful tendency for increased participation in employment, but for men, it has led to around half of men aged between 55 and 64 (ie below the official retirement age in most countries) no longer being in work. In a number of Member States, measures have been introduced to discourage early retirement, by tightening the conditions for eligibility and/or reducing the amount payable.

Encouraging partial retirement: attempts have been made (in Germany, France, Austria and Finland, especially) to encourage partial retirement by making it possible for people to receive a partial pension if they reduce their hours of work. So far, however, except in France, very few people have opted to take advantage of the possibility.

Adapting to population ageing: reform of pension systems continues to be the focus of political attention to limit the costs implied by an ageing population. In many Member States, the official retirement age has been raised, especially for women, and for both sexes is in most cases being standardised at 65, while measures have been introduced in a number of countries to reduce the pensions payable. A further tendency has been to link the pension receivable more closely to the contributions paid over a person's lifetime, so reinforcing the insurance aspect of the system. So far, there has been no general tendency to shift away from pay-as-you-go to funded schemes (from contributions covering current pensions to covering future liabilities), though there is widespread growth in occupational and private pensions.

Containing health-care costs: a common feature of recent policy developments in Member States has been to impose ceilings on expenditure of national health services or of health insurance funds. While this has generally succeeded in holding down spending relative to GDP, it has led to other concerns — about the way in which resources are effectively being rationed and the efficiency with which they are being used. In many countries, direct charges for drugs and certain services have been introduced or extended to make consumers aware of the costs involved in their supply and so encourage them to restrain their demand. In a number of Member States, governments have sought to exploit the potentially beneficial effects of market mechanisms on efficiency by separating purchasers and providers more clearly, by encouraging both to adopt more commercial attitudes and by making room for managed competition in some areas.

Providing long-term care: there is widespread debate on how caring needs should be met — whether through transfers or through the direct provision of services and how far the State should be involved. In the three Nordic EU countries, in particular, social services are well developed, though they have been increasingly subject to budget constraints. Elsewhere, adequate arrangements for helping to cover the costs of care as part of the social protection system exist in few Member States, the most notable examples being the schemes introduced in Austria in 1993 and in Germany in 1995, the former funded by general taxation, the latter by social contributions.

Targeting expenditure: Targeting resources on those most in need is of growing political concern throughout the Union. This is reflected in both the extension of means-testing — though so far in most cases this remains very limited in scale — and the imposition of taxes and/or social charges on benefit recipients, which can serve to spread the cost of funding social protection more equitably, given the increasing prosperity of many pensioners.

Modernising social protection and adapting systems to change

Systems of social protection and their reform have become a central area of policy concern across the European Union. The Commission's Communication *Modernising and Improving Social Protection in the European Union* (COM(97)102) pointed out that the financial and operational structures of most systems were established decades ago. Since then, the economic and social conditions under which they operate have changed, and will continue to do so. Demands on social protection systems have grown and constraints on their funding have tightened. This concern has been reinforced by the ageing of the population and the impending growth in the number of people of pensionable age. In the efforts to reform social protection systems, the common aims are to assure their continued effectiveness, to ensure that systems strengthen rather than obstruct economic growth and job creation, to contain the costs of providing social support to all those who need it and to shift towards a more active policy designed to get people into employment rather than merely transferring income to them when they are not working.

This new emphasis is reflected in recent European Council declarations. At Dublin at the end of 1996, the need for taxation and social protection systems to become more employment-friendly and more active in the fight against unemployment was stressed, while, at the Luxembourg Jobs Summit at the end of 1997, the Council called for a more active approach to increase the employability of those out of work. The framework for such an approach is set out in the Commission's Communication mentioned above as well as in the 1998 Employment Guidelines agreed by the Council (OJ C 30 of 28 January 1998). The main lines of action identified in the latter — improving employability, developing entrepreneurship, encouraging adaptability of businesses and their employees and strengthening the policies for equal opportunities — all have significance for the orientation of systems of social protection.

The present Report is very much focused on the themes which were the subject of the Communication and the Employment Guidelines, and which are a prominent feature of the changes being made to systems of social protection across the Union. Its specific aim is to contribute to the process of reform by reviewing and analysing these changes and so broaden understanding of the measures concerned. In part, it updates the analysis contained in the two previous *Social Protection in Europe* Reports, for 1993 and 1995 and like them is a product of the European Council Recommendation of July 1992 (92/442/EEC) to monitor the progress achieved in relation to the convergence of social protection aims and policies across the Union. (The full report is published in English, French and German; the present document which summarises the main findings is available in all 11 Community languages.)

It is based, wherever possible, on quantitative information, drawn in particular from two new sources of comparable data — the revised ESSPROS (the European System of Integrated Social Protection Statistics) on expenditure on the various elements of social welfare and their financing and the new European Community Household Panel (ECHP). The latter provides, for the first time, a comparable insight into income and living conditions in Member States, into the distribution of benefits between households and the level of income support they provide. (Both sources of data are described in the technical annex — Notes and sources — at the back of the full report and these should be consulted before drawing policy conclusions from the findings presented here.)

Outline of the Report

The Report begins by examining the changing context in which social protection systems in the Union are operating, focusing on the main demographic, social and economic developments affecting the need for support. Secondly, it analyses the scale of expenditure on social protection in Member States, its division between different functions and the relative importance of various sources of finance. Thirdly, it considers the weight of social transfers in household income and their contribution to reducing disparities in income between households. Fourthly, it reviews the major changes which have been made to social welfare systems across the Union in recent years, focusing on the period since 1995.

Four aspects of particular policy concern are analysed in some detail:

- the operation of unemployment compensation systems which in a number of Member States are being modified to give a greater incentive for people to find work;
- policy towards retirement and, in particular, towards reversing the trend for people to retire before reaching official pensionable age;
- action to contain the growing cost of health care while safeguarding the quality of service;
- long-term care for those who are infirm or too frail to look after themselves and who are imposing new demands on social welfare systems.

The changing context

While European economies are wealthier than ever before and real income, apart from brief interruptions, has continued to grow, the demands on systems of social protection have risen even more rapidly. In recent years, this has occurred, moreover, in a macroeconomic context in which, in most parts of the Union, Governments have given priority to limiting expenditure growth and consolidating public finances. (The analysis in *Competitive Europe, benchmarking the EU against the experience of Ireland and New Zealand* might help Member States decide how best to adapt their public finances and social protection systems to this new context.) Despite the growth in wealth, the scale of dependency on social transfers in most Union Member States is probably greater now than at any time during the post-war years. This seeming paradox is explained by a combination of demographic, social and economic developments which have imposed pressure on social welfare systems they were not designed to deal with.

In the first place, the population above the official age of retirement (65 in most countries) has increased in relation to the number of people of working-age and is set to rise even more dramatically in the years to come. In 1986, for each person aged 65 or over in the Union (the present 15 Member States), there were five people aged 15 to 64. By 1996, growth in the number of people of 65 and over meant that for every one person in this age group, there were only just over 4 people of working age. By 2020, on the latest projections, there will be only just over 3 people of working age in the Union for every one person aged 65 and over.

At the same time, the number of men aged between 55 and 64 no longer economically active has increased markedly, from 43% of those in this age group in 1986 to almost 50% in 1996 (the proportion of women remained much the same), largely because of the slow rate of economic growth and the inadequate rate of net job creation. If this upward trend continues, it will add to the pressure on pensions systems in future years as the growth in the relative number of people of 65 and over accelerates.

Moreover, the average age of the population of 65 and over is already increasing at the present time, intensifying the pressure on health care and social services (the average cost of providing health care alone to someone aged 65–74 is estimated to be 2–2½ times higher than for people under 65, for someone of 75 or over, 4–5 times higher). Whereas around 40% of those of 65 and over in the Union were 75 or over in 1996, by 2010, this is projected to rise to 47%, an increase of 33% in numbers in just 14 years (an average growth of 2% a year). Although total population in the Union is likely to increase by only 3% over this period, therefore, the 'healthcare-adjusted' rise is almost 10% (ie in terms of the increase in demand for health services implied by the prospective demographic change). Beyond 2010, though total population is unlikely to change much, the number aged 65 and over is projected to continue increasing, implying a 'healthcare-adjusted' growth in population of around $^1/_2$% a year.

Secondly, unemployment has increased markedly from the rates experienced in the earlier post-war years. In the Union as a whole, the average rate was consistently below 3% of the labour force throughout the 1950s, 1960s and early 1970s, whereas it has been persistently above 8% since 1982 — except in 1990, when it was only slightly lower. A significant proportion of people of working age have, therefore, been unable to obtain a job to contribute to the generation of income required to support those in retirement and have instead added to the need for social transfers.

The average duration of unemployment has also increased considerably since the mid-1970s. By the mid-1980s, the number in the Union who had been out of work for a year or more had risen to over 5% of the labour force, over half of the total unemployed. While it fell slightly between then and the early 1990s, as a result of the high rate of job growth, by 1996, the number had risen to around 5% of the labour force once more. Over $8^1/_2$ million people across the Union were, therefore, long-term unemployed at the last count and of these over 60%, almost $5^1/_2$ million, had been out of work for two years or more.

In consequence, whereas unemployment compensation systems were designed to provide income support for temporary spells of joblessness, in practice, for the last 10 years and more, at least half of those unemployed at any time were in need of longer term and, almost certainly more extensive, assistance. Moreover, the figures for long-term unemployment do not reveal the full extent of the increase in dependency. Up until recently, there was also a significant rise in a number of Member States (in the Netherlands and the UK, in particular) in men over 50 classified as disabled largely because of their inability to find a job.

The other major feature of economic developments which is relevant has been the substantial and ongoing increase in the proportion of women pursuing working careers. This trend spread first across much of Northern Europe in the 1960s and 1970s and then, in the 1980s, to the Southern Member States. In 1970, only around 40% of women aged 25 to 54 in the Union were in work or actively looking for work. By the mid-1980s, this figure had increased to 60% and by 1996, had reached almost 70%. In Spain and Ireland, the figure has risen from under 40% to 57% during the last decade alone. The effect of this has been to increase the demand not only for social support to help take care of children and elderly and frail parents or grandparents, but also for the individualisation of rights under the social protection system and for due account to be taken of interruptions to paid employment in the calculation of benefit entitlement.

This increase in demand has been reinforced by the changing structure of households and, in particular, the growth of people living alone and of lone parent families, coupled with the decline in the extended family. The average household size declined by 5% over the 10 years 1986 to 1996. This decline was common to most parts of the Union, though the average household size remains significantly larger in the Southern Member States ($2^1/_2$ people aged 15 and over per household) than in the Northern ones (under 2 per household). It is attributable, in particular, to the substantial increase in single adult households (ie with only one person aged 15 or over), which represented almost a quarter of all households in the North of the Union in 1996 as opposed to under 20% a decade earlier.

Some 8% of single adult households in 1996 had children, though in Belgium, Austria and the UK, the figure was over 12%. The great majority of the adults concerned were women, many of them in parts of the Union not in work and dependent on social transfers — in the UK, for example, some two-thirds of lone-parent families receive income support.

Moreover, in general, if someone is unemployed in the Union, there is a much higher probability that they live either alone or in a household where the other members are out of work than in one where someone else is in paid employment and, therefore, bringing in income. In 1996, 15% of households in the Union with a working-age adult had nobody in work. In Belgium, Finland and the UK, the figure was 20% or more, much higher than the average rate of unemployment. In the UK, where unemployment fell significantly over the 10 years 1986 to 1996, the proportion of households where nobody was in work rose, while in Ireland, where unemployment fell by even more, the proportion remained unchanged.

The main quantitative findings

The scale of social expenditure

Any assessment of the scale of social protection in European countries, and the associated cost in terms of the transfers involved, can only satisfactorily be made by considering the revenue side of the public sector accounts as well as expenditure. This is, first, because social transfers are increasingly subject to tax or social charges in a number of Member States and, accordingly, part of the expenditure incurred by government returns as tax or other receipts. Secondly, effective transfers can, in principle, be made through tax concessions or allowances as well as through benefit payments and, in this case, will show up as lower receipts rather than as expenditure. Estimating the scale of such so-called tax expenditures and the revenue generated by taxes on benefits is, however, fraught with difficulty.

So far as expenditure is concerned, social protection (as defined under the new ESSPROS to include social transfers, either in cash or in kind for welfare purposes, and health care) amounted to 28½% of Union GDP in 1995. This figure, however, varied markedly between Member States, ranging from 20% of GDP in Ireland, 21% in Greece and Portugal and 22% in Spain, to 30% or more in France, the Netherlands and the three Nordic Member States, with Sweden showing the highest figure at just under 36% of GDP (Graph 1). For the rest, in Belgium, Germany and Austria, expenditure was just under 30% of GDP, while in the UK, it was around 27½% and in Italy 24½%. (Because of the newness of the system of classification, these figures are provisional and liable to change as better information becomes available — see Notes and sources in the main report.)

The variation in these figures between Member States are broadly in line with relative levels of prosperity, as measured by GDP per head, and, therefore, reflect the ability of countries to support the expenditure concerned. Nevertheless, it is evident that there are differences between countries with similar levels of prosperity in the implicit priority accorded to social protection. This, in turn, partly reflects differences in social characteristics (in the tendency for women to pursue working careers, for example, which is high in the Nordic countries and low in Italy), in the age structure of the population and in the degree of reliance on private provision (private pensions are included to varying extents in the ESSPROS data depending on the degree of social solidarity involved).

In a number of the countries, however, especially in those where social spending is high in relation to GDP, benefits are subject to tax and/or social charges, so that part of the money paid out by government comes back as receipts on the revenue side of the accounts. This part, moreover, has tended to increase in recent years as governments have sought both to target protection more effectively on those most in need of support and to distribute the costs more evenly.

According to a recent study ('Net public social expenditure', *OECD, Labour Market and Social Policy Occasional Papers, No. 19*), direct taxes and social contributions levied on benefits amounted to almost 6% of GDP in the Netherlands, over 5% in Sweden, 4% in Denmark and 2½% in Germany, whereas in the UK, the figure was virtually zero. Taking account also of the revenue from indirect taxes as beneficiaries spend their transfers — which is more similar between countries — reduces expenditure on social protection in net terms to around 27% of GDP in Sweden and to between 23% and 25½% of GDP in the other four. This is much less of a difference than shown by the gross spending figures noted above. Moreover, in net terms, the UK is estimated to have slightly higher expenditure relative to GDP than Germany and the Netherlands.

These estimates relate to only five Member States for a single year (Eurostat plans to develop special modules on the effects of taxes as part of ESSPROS) and are somewhat tentative. A further insight into the relative weight of social transfers can be gained from the ECHP data on net benefits received by households. Benefits in this case are confined to cash transfers and exclude benefits in kind, such as health care, though they include all private pensions. According to these data, social transfers amounted, on average, to just over 30% of net household income in the Union in 1993 (the Union here excludes Austria, Finland and Sweden which were not covered by the first wave of the ECHP).

The pattern of variation between Member States differs from that shown by the figures for gross expenditure relative to GDP. Social transfers were highest in Belgium and France, at over 36% of net household income (though the figure for France is slightly overstated because transfers are measured gross of the relatively small amount of tax payable on them), and next highest in Italy, which is well below the Union average in terms of the expenditure figures, at just under 33%. They were similar to the average in Denmark and the Netherlands, as they were in Spain, where, like Italy, the ratio of expenditure to GDP is relatively low, below average in Germany, Ireland, Luxembourg and the UK (at around 27% of net income) and lowest, in Greece and Portugal (25% and 22%, respectively), in line with the expenditure figures.

So far no reliable estimates are available for the overall value of tax-expenditures and their exclusion is liable to distort the comparative picture which emerges from the ESSPROS and ECHP data, though the amounts involved seem in most cases to be relatively small (though there are exceptions, such as the UK where tax relief on private pension contributions is important).

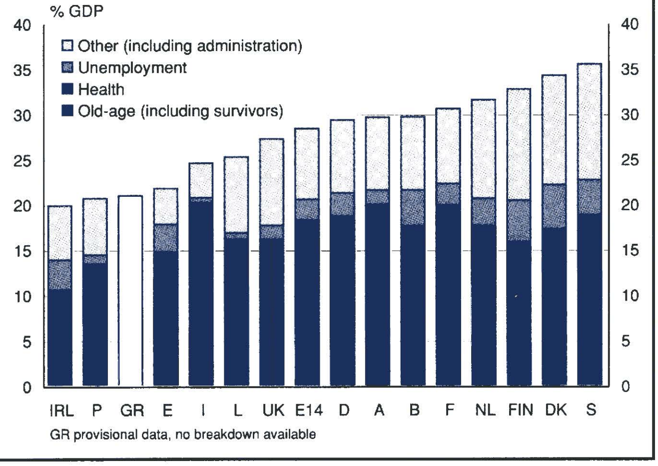
The pattern of social expenditure

Old-age pensions are by some way the largest item of social protection expenditure in the Union, accounting for 42½% of the total in 1995, equivalent to 12% of GDP. The figure, however, varies from over 60% in Italy (15½% of GDP) — far more than in any other Member State (but include some transfers allocated to other items in other countries) — to 32% in Finland (10½% of GDP) and only 25% in Ireland (5% of GDP). In the latter, this partly reflects the small proportion of the population above retirement age, just as the high figure in Italy reflects the opposite, though here the large numbers retiring early reinforces the unfavourable age structure.

While, in general, high unemployment is often regarded as a primary cause of high levels of social spending, in reality, transfers to the unemployed accounted for only 8% of total expenditure in the Union in 1995 (just under 2½% of GDP) — less than spending on disability benefits and only a little higher than that on family allowances. Only in Belgium, Denmark, Finland and Sweden, was expenditure on unemployment benefits significantly above 3% of GDP (4–5% in each case).

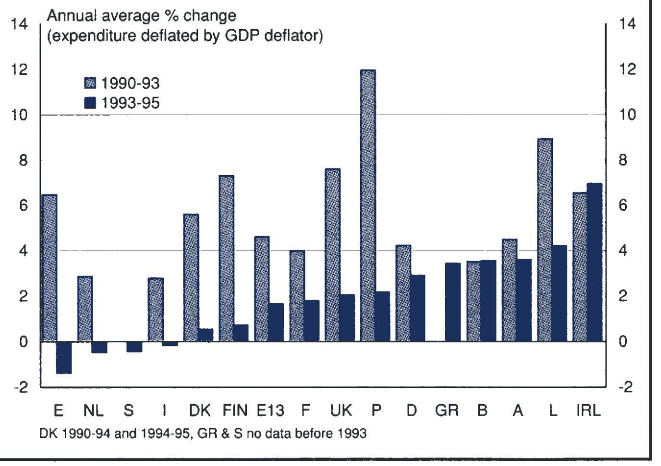
At the same time, such expenditure is only a very partial indicator of the costs of unemployment for systems of social protection. Not only does it reduce the finance available from taxes and contributions, but it also adds to spending in other areas. Part of spending under disability benefits, housing allowances and social exclusion is also, in practice, related to unemployment — or, more generally, to job shortages — as is a large part of spending on early retirement

1 Total expenditure on social protection by broad function in Member States, 1995



GR provisional data, no breakdown available

2 Growth of social expenditure in real terms in Member States, 1990-93 and 1993-95



DK 1990-94 and 1994-95, GR & S no data before 1993 pensions (which are included as part of old-age pensions in about half the Member States rather than unemployment compensation, as required under the ESSPROS classification). In the Netherlands and the UK, expenditure on disability benefits was much higher than on unemployment benefits in 1995 ($4^1/_2$% of GDP and 3%, respectively), while spending on housing and social exclusion amounted to another 1% of GDP across the Union (over 2% of GDP in Denmark, Sweden and the UK).

Health care is the second largest item of expenditure, amounting to around 22% of the total in the Union, as well as in all Member States, except for Denmark (only 14%), and to some 6% of GDP, though varying from under 5% in Denmark and Italy to $7^1/_2$% in France, well above the figure in any other Member State.

The growth of social expenditure

Total spending on social protection increased from just under 26% of GDP to $28^1/_2$% over the five years 1990 to 1995 as compared with a rise of around 1% of GDP over the 1980s (on the previous ESSPROS definition). The increase was common to all Member States with the sole exception of the Netherlands, where there was a small fall. (Unfortunately, no estimates are available for the change in net terms, which is likely to have been less.)

The rise, however, reflects in large measure the slowdown in GDP growth itself during the 1990s — to under $1^1/_2$% a year as against almost $2^1/_2$% in the 1980s. Moreover, the rise was confined to the period 1990 to 1993, the years of recession when there was very little growth at all in GDP. In the two years 1993 to 1995, social spending in the Union declined on average relative to GDP, rising only in Belgium, Germany and Austria and falling elsewhere. While this was partly due to some recovery in GDP, it was also the result of a marked slowdown after 1993 in the growth of social protection itself, to some extent reflecting the stabilisation of unemployment after the large rise which occurred during the recession years.

In real terms (adjusting for general inflation), social spending grew by an average of around $4^1/_2$% a year in the Union in the three years 1990 to 1993, when GDP hardly increased at all. In the two years, 1993 to 1995, it went up by $1^1/_2$% a year (Graph 2). Only in Belgium and in Ireland (where GDP rose by over 9% a year) was there no reduction in the rate of real growth over the latter period. Even after excluding unemployment benefits, which declined in real terms between 1993 and 1995, average expenditure growth after 1993 was half the rate in the three years before.

The largest rise in social expenditure over the five years 1990 to 1995 (6–7% of GDP) occurred in Portugal, where efforts were being made to raise protection to the standards in the North of the Union, and Finland, where unemployment rose more steeply than anywhere else. By contrast, in the Netherlands, expenditure fell slightly relative to GDP, while in Ireland and Italy, the rise was well below average (under 1% of GDP), in the former, GDP and social spending growing strongly, in the latter, both growing slowly.

Apart from unemployment benefits, old age pensions and health care showed the largest rise over the period (up by 1% of Union GDP and $^1/_2$% respectively), in part reflecting the ageing of the population. Between 1993 and 1995, however, spending on health care fell relative to GDP in a number of countries, while that on old-age pensions rose in line with, or less than, the growth in GDP in most Member States.

Sources of finance

The funding of social protection continues to be the focus of much policy attention. The emphasis throughout the Union, as part of the attempt to increase job creation, has been on reducing non-wage labour costs. This objective, proposed by the Commission in its White Paper on *Growth, Competitiveness and Employment* in 1993, was confirmed by several European Councils, especially in Dublin at the end of 1996, as well as in the Employment Guidelines adopted at the end of 1997. However, so far there is little sign that the level of charges levied on labour (taxes and social contributions) has decreased. In fact, the implicit tax rate is estimated to have increased from 35% in 1981 to 42% in 1995. (Improvements in the coordination of taxation policies across the Union to address this issue are currently being discussed by the Taxation Policy Group set up be the European Council in Dublin at the end of 1996.)

The funding for social protection in all Member States comes partly from social contributions, levied mostly on income from employment, and partly from general taxation, though in a few countries (Belgium, France and Luxembourg, in particular) 'earmarked' taxes have been introduced in recent years. On the latest figures (for 1995), around 65% of finance in the Union still comes from contributions, some 60% of these paid by employers, including voluntary as well as statutory contributions (ie 40% of total funding), and 30% from taxation, virtually all of this from general taxes.

The relative weight of the two broad sources varies between countries, reflecting the historical development of the system itself. In Member States where the system has its origins in the provision of social insurance for those in employment (the so-called Bismarkian system) — the Benelux countries, France, Germany and Austria — social contributions still account for two-thirds or more of funding (as much as 77% in France). In the Nordic countries, the UK and Ireland, where the system has its origins in the provision of social welfare for those in need (the so-called Beveridge system), social contributions account for less than half of total finance (40% or less in the UK and Ireland and only 23½% in Denmark). In the South of the Union, two-thirds or more of revenue comes from contributions in Greece, Spain and Italy, but just under half in Portugal.

In all countries, except Denmark and the Netherlands, a much larger share of contributions comes from employers than from those being protected. In line with stated policy aims, however, there has been some shift to other sources during the 1990s. In the Union as a whole, the revenue raised from employers' contributions declined from 43% of the total to 39½% in the five years 1990 to 1995, while that raised from those protected rose from 22½% to 23½%. This shift was common to all Member States, except for Denmark and the Netherlands, where employers' contributions are relatively small, and Belgium. It was especially marked in Portugal and Finland, where revenue from employers' contributions was reduced by some 20% in relative terms.

In relation to labour costs, however, the evidence suggests that employers' contributions increased slightly between 1990 and 1995 across the Union, while they remained virtually unchanged relative to GDP, despite their decline as a share of total funding for social protection. Though governments have sought to relieve employers of some of the costs of financing social protection, therefore, this aim has generally been frustrated by the growth of expenditure — and funding requirements — at a higher rate than GDP and, accordingly, than the tax base from which revenue has to be raised. The increase in employers' contributions relative to labour costs (or the overall wage bill as measured by the compensation of employees) was common to all Member States for which data exist (ie excluding Greece, Luxembourg and Sweden), except Portugal and Ireland.

The other main development on the funding side, apart from the emergence of earmarked taxes, which is limited to a very few countries (in France, their share of revenue rose from 3½% in 1990 to 8% in 1995), is the increase in contributions levied on old-age pensioners and other benefit recipients. This reflects both the growing real income of pensioners and the desire to spread the cost of financing more evenly across the population. Nevertheless, only in the Netherlands (8½%) and Germany (4%) are they a significant source of funding.

Levels of unemployment benefit

Data from the ECHP for the first time enable the actual level of benefit received by those out of work to be compared across the Union (whereas previously it has been necessary to rely on the results of models — see *Social Protection in Europe, 1995*, Chapter 4 — which however well they capture the features of the benefit and tax systems in operation provide no indication of how representative the results for hypothetical cases are in reality). They indicate that, in practice, the disincentive to look for work associated with the benefit system seems to vary markedly across the Union. In the first place, around a quarter of those aged 25 to 64 in the Union in 1993 who were unemployed for at least three months received no unemployment benefit at all (though they may have received other means of support to ensure that their income did not fall below a minimum level). This proportion, however, varied from 5% or less in Belgium, Denmark, Germany and the UK and only slightly more in Ireland, to around two-thirds in Greece, Italy and Portugal (in the

ECHP no comparable data exist for the Netherlands, Austria, Finland and Sweden and there are insufficient observations for Luxembourg).

Secondly, for those receiving benefit, the monthly payment averaged just over 50% of net earnings for the months that they were employed (which, it should be emphasised, could be in the jobs they moved into after they were unemployed as well as in the jobs they had before becoming unemployed), but was over 75% in Portugal (though only a third of the unemployed received anything) and around 60–65% in Denmark, France and Ireland, but only 25% in Greece and the UK (Graph 3). Benefit levels in Belgium and Germany were around the Union average, in Spain just above and Italy below. (It should be emphasised that these figures relate only to benefits linked with unemployment and the people concerned may also be in receipt of other transfers which might affect the level of benefit relative to earnings — see Chapter 4 of the full report.)

Thirdly, the proportion of the unemployed receiving benefits of 80% or more of their net earnings when in work (assuming that their average monthly earnings calculated from the ECHP data reflect the pay they receive in the jobs they move into after being unemployed), was relatively small in most of the Member States covered (around 20% or less of men in 8 of the 10 countries, all except Ireland and Portugal and under 6% in Greece, Italy, and around 20% or less of women in 7 of the countries, though around a third in Germany and France and half in Denmark).

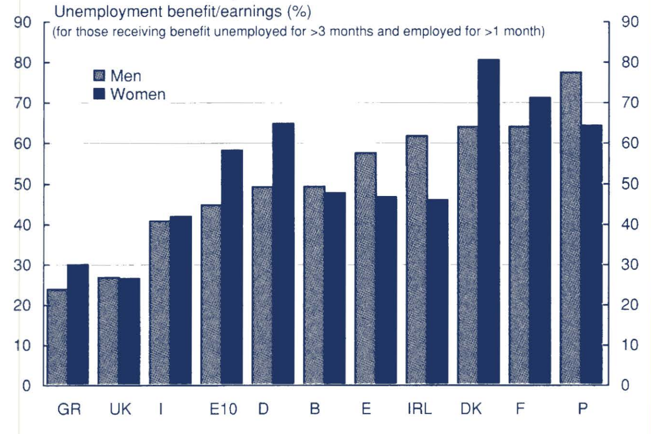
These figures need to be interpreted with some caution, however, since in a number of countries where benefit levels are low (the UK especially), various benefits in kind not included in the ECHP data, such as housing allowances, are also payable to those unemployed to supplement their income (it is also important to take account of the nature of the data, which is explained in Chapter 4 and Notes and sources in the full report). Nevertheless, though significant, these additional payments are unlikely to alter the picture substantially, partly because in many cases they are also payable to those in low-paid jobs, which most of the unemployed tend to go into when they return to work (the ECHP indicates that monthly earnings of those unemployed for part of 1993 were in most cases substantially below average — see Chapter 4 of the full report).

The relief of poverty

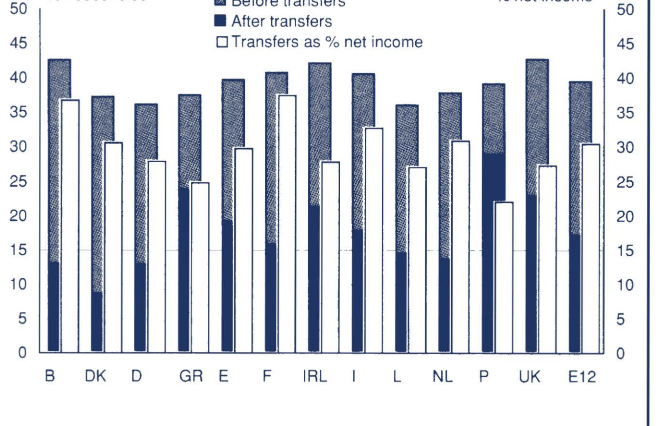
As constraints on social expenditure tighten, the concern in all Member States is increasingly to allocate revenue in the most effective way. Data on household income from the ECHP provide an insight into the extent to which transfers are targeted on the poorest in society and, as a result, succeed in alleviating relative deprivation and narrowing disparities in income distribution, though it should be stressed that this is only one of the aims of systems of social protection in the Union.

According to the ECHP, social transfers (including private pensions) in

3 Average unemployment compensation relative to earnings for men and women aged 25-64 in Member States, 1993



4 Scale of social transfers and effect on households with net income below 50% of average, 1993



the Union accounted for around 30% of net household income in 1993, as noted above. For some 37% or so of households, they represented the main source of income. In their absence, almost 40% of households would have had an income level of under 50% of the national average (a measure conventionally used as an indicator of relative poverty and agreed as a working definition by the Council of Ministers in December 1984), many none at all. This proportion varied comparatively little between countries. In Belgium, Ireland and the UK, it was around 42%, in Denmark, Germany, Greece, Luxembourg and the Netherlands, 36–37% (Graph 4).

After transfers, and after tax, an average of around 17% of households in the Union had an income level below half the national average. In the UK, Ireland and Greece, the proportion was over 20% and in Portugal, some 29%, in Spain, France and Italy, it was around the Union average (15 to 19%), in the Benelux countries and Germany, 13–14% and in Denmark, under 9%. The effect of transfers in reducing the share of households with income below 50% was greatest in Belgium and Denmark, where the reduction was around 29 percentage points, though Denmark achieved this with proportionately smaller transfers (30% of net household income) than Belgium (37%). The effect was also relatively large in France and the Netherlands (24–25 percentage points), though in France, the scale of transfers was similar to that in Belgium (even allowing for the overstatement of transfers in France noted above) and in the Netherlands, similar to that in Denmark.

By contrast, the reduction in the share in Greece was only 14 percentage points and in Portugal, only just over 10 percentage points. In terms of the scale of social transfers (25% of net household income in the former, 22% in the latter), the effect in relieving poverty in the two was very similar and in both transfers appear to be less targeted on the poorest than in other Member States (around 70% of transfers going to households with under half average income before transfers as against 77% in the Union as a whole).

Over the rest of the Union, the reduction in share was 20–23 percentage points, though again the level of transfers involved in achieving this differs between countries, being higher in Italy, for example, than in Germany (23 percentage points as against 20).

The comparatively small effect of social transfers on income distribution in Greece and Portugal also reflects their uneven allocation between households, with some receiving a substantial amount, others comparatively little. This was particularly so in the case of old-age pensions which are the major element in transfers, though it also applied to other transfers (unemployment benefits, family allowances and so on), as it did in Italy. In the case of these other transfers, over the Union as a whole, 19% went to the 17% of households with income below 50% of average after transfers and 37% to the 30% with income below 65% of average.

In the case of old-age pensions, on the other hand, 19% of transfers went to the 15% of households in the Union with income of over $1^1/_2$ times the average after transfers (28% in Greece and Portugal to the 16–17% of the households in this category, 25% in France to the 13% of households and 29% in the Netherlands to the 15% of households). In four countries, however, Belgium, Ireland, Luxembourg and, most especially, Denmark, pensions went disproportionately to lower-income households.

Recent changes in policy

The common response of governments across Europe to the expenditure trends noted above, has been to seek ways, on the one hand, of containing the growth of spending and, on the other, of activating policy to reduce the number of people dependent on social transfers. The activation of policy has been a central theme underlying many recent reforms, the aim being to shift from a passive stance of income support to an active one of encouraging those out of work to take up paid employment, by increasing incentives to work and helping people to participate in society and working life. Measures have, therefore, been implemented to improve the employability of those out of work, to provide access to training and career guidance and to assist them in finding a job.

This approach has not been confined to those registered as unemployed but has been extended to other groups dependent on long-term state support, especially to people with disabilities but potentially able and wanting to work, lone parents and those retiring from work early. The aim has been not just to reduce dependency and expenditure, but to combat social exclusion by helping the people concerned find a more meaningful place in society and a chance to contribute to its well-being.

The ageing of the population has added further impetus to these efforts. It has also served to focus increased attention on the growing costs of health care, which goes disproportionately to the elderly, and on the need for new ways of catering for those requiring long-term care.

The concern to address this new need exemplifies the prevailing attitude towards social protection across the Union. Although the emphasis is on cost containment and reducing expenditure wherever possible, the principle of maintaining a universal system which provides protection to all those in need remains unquestioned. Nevertheless, there is increasing debate on how widely social welfare systems should extend, what risks they should cover and, most pertinently, where state responsibility should end and individual responsibility take over. At the same time, there is a growing emphasis on the pursuit of active measures and the need to support policies for increasing employment, the main guidelines of which were agreed by Member States at the Luxembourg Jobs Summit.

Tightening eligibility for benefit

In several Member States (the Netherlands and Sweden, in particular), the qualifying conditions for benefit have been tightened since 1993 (the year to which the analysis above relates), while in others (Spain, Austria and Finland), the contributions record required to be eligible for benefit has been lengthened. Rates of benefit have also been reduced, as in Germany and Finland — in the latter by their non-indexation in 1995 and 1996. On the other hand, in Sweden, although the rate of benefit was reduced from 80% to 75% in 1996, after being lowered from 90% before that, the rate was restored to 80% in 1997.

The period of entitlement to insurance benefit has also been shortened in some Member States — in the UK, from one year to only 6 months on the introduction of the Job Seeker's Allowance in 1996 (payment being means-tested after that); in Denmark, from 9 years to 7 years in 1995 and to 5 years in 1996, though it remains among the longest in the Union (but for the last 3 years, intensified efforts are made to get the unemployed into active programmes). In Belgium, from 1996, benefits can be withdrawn if the person concerned has been unemployed for more than 1½ times the regional average (instead of twice as long as before).

Strengthening incentives to work

Cuts in benefit and a tightening of eligibility criteria provide in themselves an increased incentive to work. Other measures have also been introduced in a number of countries to make it more attractive, and in some cases more feasible, for people to work rather than remain unemployed. In-work benefits, designed to increase the take-home pay from working, even in low-paid jobs, exist, at present, in only the UK (eg Family Credit) and Ireland (Family Income Supplement). Whereas so far they have been paid only to people with children, in the UK, a pilot scheme was introduced in 1996 for low-paid workers without children. In both countries, the number of people covered by in-work benefits has increased in the recent past as qualifying income levels have been raised. Lone parents have been targeted specifically, with a new benefit for these being introduced in Ireland in 1997. Help with child care for low income families, including lone parents, was also introduced recently in the UK. In the latter and elsewhere, attempts have been made to encourage the unemployed to take part-time jobs, partly to prepare them better for full-time employment — through giving them entitlement to unemployment benefits (in Belgium, or enabling them to keep some of their benefit in the UK).

Effects similar to those of in work-benefits can be also obtained by granting specific tax advantages for low-wage earners (eg in Finland, measures have been introduced to reduce the income tax paid by those on low pay, a concession which is withdrawn as earnings increase).

Shifting towards more active policies

Changes in unemployment compensation systems have generally been accompanied by measures aimed at increasing the employability of the unemployed and helping them find a job, including, for example, training to improve skill levels in line with labour market requirements and advice on job search and interview techniques. Shifting policy from passive measures of income support to active measures, however, is not so easy, especially during periods of high unemployment. Given budget constraints, it requires a restructuring of expenditure and a reform of benefit and tax systems to maximise the return on existing outlays. Although the need to shift expenditure from passive to active labour market measures was highlighted by Member States at the Essen Summit at the end of 1994 and reiterated at successive Council meetings since, the policy intention has been slow to show up in the figures on labour market expenditure. Between 1990 and 1996, there was only a small rise in the Union as a whole in spending on active in relation to passive measures, all of which has occurred since unemployment stabilised in 1994 (Graph 5). Member States have, therefore, reaffirmed their commitment to bring about such a transition in the Employment Guidelines agreed at the Luxembourg Jobs Summit.

In a number of Member States, conscious efforts have been made to improve the articulation between the provision of income support and getting the unemployed into work. In Denmark, as noted above, measures were introduced in 1995 to ensure that anyone unemployed for two years either receives a job offer or goes on a training course, which seems to have been a key factor in reducing unemployment to under 6% at the last count as against over 8% in 1994. At the same time, those under 25 with insufficient education or training have a right to education or training for at least 18 months if they have been unemployed for six months but forfeit the right to receive unemployment benefits if they do not take up the offer. In Sweden, a new programme was launched in 1996 to draw up individual action plans for job-seekers, who are able to take a year off to study while effectively receiving unemployment benefit. In the UK, a key element of the Job-seeker's Allowance, introduced in 1996, is a requirement for the unemployed to enter into an agreement specifying the steps they intend to take to find work and the services available to help them.

These programmes exemplify the increasing importance attached to providing job-search assistance to the unemployed as well as access to training or re-training courses. This importance was emphasised at the Luxembourg Jobs Summit and is a prominent feature of the Employment Guidelines agreed by Member States, which specified that:

- every unemployed young person should be offered a new start before reaching six months of unemployment, in the form of training, retraining, work practice, a job or other employability measure;
- unemployed adults should be offered a fresh start before reaching twelve months of unemployment through one of the above measures or, more generally, through individual vocational guidance.

Despite the acknowledged importance of training, however, only a small minority of the unemployed at present receive training in the Union, a situation which Member States also committed themselves to improving in the Employment Guidelines (setting a specific target of increasing the proportion to 20%).

Extending job creation schemes

In several Member States, job creation schemes are under discussion. Any assessment of the cost-effectiveness of these schemes, however, has to take account not only of the direct effect on jobs of the measures introduced but also their substitution effects (employers dismissing workers and taking on subsidised ones in their place) and deadweight costs (employers recruiting subsidised workers they would have taken on anyway).

In a number of Member States, job creation has been encouraged through selective reductions in the social contributions levied on employers as well as by direct subsidy. In Belgium, employers creating jobs for young people and long-term unemployed in socially-useful activities ('Smets jobs') receive both a large subsidy for three years and full relief from social contributions. In the UK, employers taking on people unemployed for two years or more are exempt from social contributions for a year, while in France, recruitment of the long-term unemployed is subsidised both directly and through reductions in contributions. The new French Government, moreover, is diverting the resources at present going to a range of job subsidies into plans for creating 700 thousand jobs for young people at the minimum wage.

More generally, Member States recognised at the Luxembourg Jobs Summit the potential importance of job creation at the local level in the social economy and in new activities where needs are not being satisfied by the market (eg in the environmental sector). They agreed in the Employment Guidelines to investigate measures to exploit these possibilities and to identify and, where possible, remove obstacles to their development.

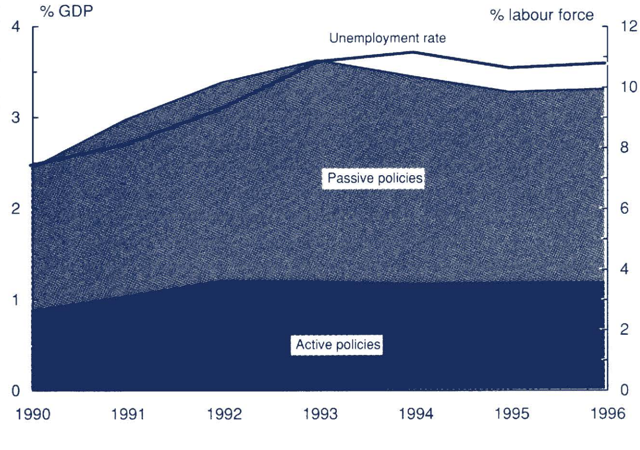
Reducing dependency and social exclusion

In all Member States, social assistance is available to those unable to work for one reason or another, though in some countries, in the South of the Union, in particular, a minimum level of income has not been universally available. In Italy, there is a political discussion whether to establish a national (in place of a regional) means-tested minimum income scheme, with payments related to family size, as recommended by the Onofri Report. In Portugal, a minimum-income guarantee scheme was introduced in 1997, involving not just the provision of income support but measures to help recipients integrate into society. This is a response to the experience under longer-standing schemes elsewhere, where social transfers by themselves have not proved sufficient to overcome the problem of deprivation and social exclusion.

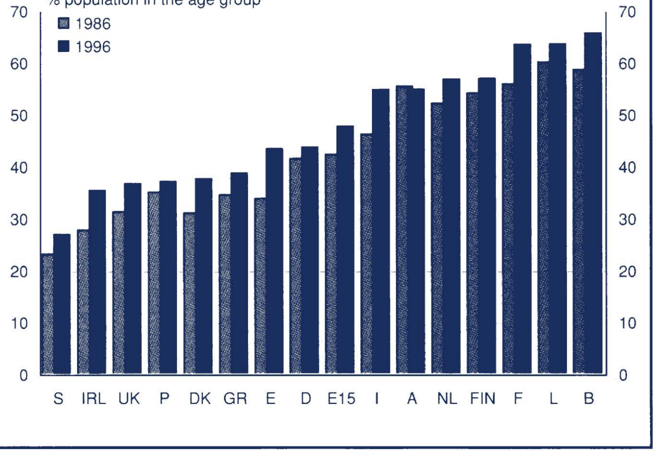
Indeed, a general tendency throughout the Union is to address the underlying causes of poverty and social exclusion and to avoid systems of income support becoming the means for entrenching a permanent division in society between those who contribute to its well-being and those who do not. The aim, in particular, is to help those dependent on benefits to become more self-supporting by giving them an opportunity to find a job, which means not just providing access to training and job counselling but to accommodation and adequate levels of health care and social services, such as child care facilities.

In Denmark, from 1998 on, everyone receiving social assistance will be given the chance to return to education or go on to a training scheme. In Germany, increased efforts have been made to get those on social assistance into active labour market programmes, while in the UK, the new Government has announced a 'welfare to work' programme aimed at reducing the number of people reliant on benefits. The latter is particularly focused on the young, the long-term unemployed, people with disabilities and lone parents. From October 1998, all lone parent who wish to work will have access to personal advice from the employment services as well as receiving assistance with child care. At the same time, however, additional benefits available to lone parents will be withdrawn for new claimants and the same level of benefit will be payable to all those with children. In the Netherlands, in similar vein, more stringent procedures for claiming so-

5 Expenditure on active and passive labour market policies in the Union, 1990-96



6 Men aged 55-64 no longer in the labour force in Member States, 1986 and 1996



cial assistance have been introduced, requiring recipients to be actively seeking work and to accept any suitable job offer they receive, except if they are lone parents with a child under 5. In Luxembourg, recipients of support are required to have exhausted all other means of improving their situation and be actively seeking employment, unless they are 50 or over or disabled.

Helping people with disabilities

Attempts have been made across the Union to reduce the number receiving disability benefits by introducing more stringent tests for assessing incapacity for work. In the UK, a tougher medical test, which after 28 weeks on benefit is designed to assess a person's fitness to do any kind of work rather than their previous job, has been introduced, much the same as in Germany, where benefit entitlement depends on people being incapable of working at all. In the Netherlands, the financial responsibility for disability benefits has been shifted to employers whose contribution rates are now — partly — differentiated according to the number of their employees claiming disability benefits, a measure which gives an incentive both to improve health and safety at work and to continue employing those with disabilities. This has been coupled with greater stress on helping people with disabilities, but able and wanting to work, to find jobs through active employment programmes. In Austria and Finland too, the emphasis of policy has shifted from income support to rehabilitation, with entitlement to benefit needing to be re-established periodically.

Incentives for people with disabilities to look for work and help for them to do so have generally been accompanied by legislation to prevent discrimination against them in employment and in their access to goods, services and facilities of various kinds as well as by enabling measures, especially in the work place, to remove obstacles to them working — in 1993, all Member States adopted the UN *Standard Rules of Equality of Opportunity for Disabled People*. Such measures, however, while increasing equality of opportunity, will only result in additional competition on the job market, where those with disabilities will always be disadvantaged, unless there is, at the same time, sufficient growth of employment.

Reversing the trend towards early retirement

The tougher stance on disability benefits, which in many cases have been paid to those over 50 losing their job, is part of a reversal of policy towards older workers, towards encouraging them to stay in employment rather than retire early (except in agriculture where early retirement continues to be promoted under Regulation 2079/92) and represents a reaction to the fact that in 1996 almost half of men aged 55 to 64 in the Union were no longer economically active (Graph 6). Because of job shortages, however, there remains an awkward conflict between increasing the number of older people in work and reducing unemployment (though this conflict disappears once the focus of policy is, more satisfactorily, on the employment rather than on the unemployment rate, as in the Employment Guidelines).

In addition to the examples noted above, those claiming early retirement pensions in Sweden now need to demonstrate that they are incapable of working, in effect, transforming the payment into an invalidity benefit, while, at the same time, the basic rate has been reduced. Eligibility criteria have also been tightened and the pension effectively reduced in Germany and Austria, coupled in the latter with an increase in the required period of contributions from 35 years to 37½. In Belgium, the number of years of contributions necessary to qualify for a pension is being raised gradually from 20 to 35 beginning in 1997, while social contributions on early retirement pensions have been increased. In Spain, voluntary retirement before the age of 65 is now penalised, while in Greece, pensions payable to those retiring early have also been reduced.

Moreover, in Austria, further encouragement to employment of older workers has been given by a *bonus-malus* scheme, reducing social contributions for employers taking them on and imposing a penalty on those dismissing them.

Encouraging partial retirement

One means of diminishing the conflict between providing jobs for older workers and reducing unemployment is to encourage people to move from full-time to part-time employment as they approach retirement age. This, moreover, can ease the transition process for those concerned while taking extended advantage of their experience and know-how. Partial pensions to this effect have been introduced in a number of Member States in recent years. Elsewhere, however, obstacles exist for older workers wishing to work part-time (in the UK, for example, they cannot continue to work for the same employer if they draw an occupational pension).

In Austria, a partial retirement scheme has existed since 1993, enabling people to reduce hours of work and receive a proportion of the pension normally payable, though few people have opted for it, seemingly because early retirement *per se* is more attractive. In Finland, a similar scheme has existed since the end of the 1980s, but again the number involved has been small. In Germany, partial retirement has been introduced more recently for those of 55 and over, at the same time as their eligibility for early retirement was restricted. The possibility of combining a partial pension with a partial salary also exists in Luxembourg, though relatively few fewer people have so far taken up the option. More success has been achieved in France, where partial retirement has been regarded since 1993 as a solution to (full) early retirement and where the number opting for the latter has fallen while those continuing to work part-time have risen (to 27,000 in 1995).

Adapting to population ageing

The reform of pension systems, aimed at managing the cost of the impending growth in population of pensionable age — or, more accurately, the income redistribution entailed — has become a central policy aim in all countries. (The pension reforms in Italy, Sweden and France in particular were described in detail in *Social Protection in Europe, 1995*, Chapter 2, while a general economic analysis of pension reform and the future of the welfare state was recently published in *European Economy, Reports and Studies*, 4/1997.) A common response has been to raise the official retirement age of women to conform with that of men, for both cost and equity reasons — as in Germany, Greece, Portugal, the UK, and, more recently, in Belgium and Austria. In all these countries, as in most other parts of the Union, the official retirement age is being standardised at 65. This, however, is being coupled with increased emphasis on the contributions record of those retiring, so linking the pension received more closely with the payments made over a person's working career and reinforcing the insurance aspect of the system.

In addition, the effective pension payable relative to past earnings has been reduced in a number of countries by altering the calculation formula. In France, Portugal, Austria and Finland, the number of years of earnings on which the pension is based has been increased, while the method of revaluing pensions for inflation has been made less favourable, as has also occurred in Spain, Germany (through a shift in the basis from gross to net earnings) and Sweden (where pensions are not being fully indexed so long as the budget deficit remains excessive).

In other countries, the value of pension has been reduced more directly. In Greece, the rate of supplementary pension relative to earnings has been reduced and limits set on the maximum payable, resulting in a rise in pensioners receiving very low incomes and prompting the introduction in 1996 of a means-tested allowance. A similar allowance has also been recently introduced in Spain, where the number of years needed to qualify for a full pension has been raised and the coefficient applied to earnings reduced. In Germany, the new pension reform to take effect from 1999 introduces a 'demographic factor' into the pension formula to take account of the increasing life expectancy of pensioners and accordingly to reduce the standard pension (*Eckrente*) from 70% of previous net earnings to 64% by 2030, in addition to raising the pensionable age.

So far, however, there has been no general tendency to shift away from pay-as-you-go to funded schemes (ie from contributions covering present pension liabilities to covering future ones), though there is a widespread growth in the importance of occupational and private schemes to supplement basic pensions and relieve the State of part of the future funding liability. As emphasised in the recent Commission Green Paper on *Supplementary pensions in the single market*, (COM(97) 283), the growth of such supplementary schemes requires an appropriate Community-wide framework. The Green Paper also notes that the sustainability of pay-as-you-go schemes necessitates further reform of pension systems. Although reversing the trend towards early retirement can alleviate funding problems, it is unlikely to solve them completely. In this regard, it is relevant to note that there is a shift towards defined contribution systems, where contributions paid over a person's working career determine the amount received in pension, so reducing some of the difference between pay-as-you-go and funded systems.

The only two countries in the Union where funded pension systems play a major role are the Netherlands and the UK. In the latter, in particular, where the basic state benefit is lower than in most other Member States, two-thirds of pensioners have an occupational or private pension. The State concentrates on taking care of the less well-off, leaving the management of pension funds largely to private insurance companies. The main recent focus of policy has been on strengthening the regulations governing these funds, to prevent their fraudulent use and the misleading selling of private schemes.

Whether a funded approach is better designed to overcome the transfer problem inherent in demographic trends remains unclear. Ultimately, the ease of securing the transfer of income from those in work to those in retirement, irrespective of how it is achieved, depends largely on the income available to be distributed and, therefore, on the economic growth sustained in the intervening period.

Containing health-care costs

The ageing of the population, together with constraints on public expenditure, has also focused policy attention on health care, the demand for which in any event tends to rise rapidly as real income increases and medical know-how expands. The widespread response in Member States has been either to limit expenditure directly where services are managed by the state or to impose ceilings on spending growth where this is determined by health insurance funds. While this has generally succeeded in holding down spending relative to GDP in recent years, it has given rise to other policy concerns — in particular, how best to allocate expenditure to serve the needs of society as a whole and how to ensure that available resources are used efficiently.

It has, in addition, raised more fundamental questions about the relationship between public and private health sectors, about whether the former should be limited to basic care — and, if so, how this should be defined — and about the implications of this for the overall pattern of care in relation to need (and the possibility of a shift from essential to more cosmetic treatment). It has also given rise to questions about the justifiability of limiting the growth of services (and jobs) to below the level people seem willing to pay for and, in turn, about how far consumers can be relied on to make rational choices on an issue which is so important but about which there is a serious lack of information.

The tendency in most Member States has been to seek to exploit the advantages of the market while retaining control over supply. In particular, people have been encouraged to consume less and choose more rationally by making them aware of the costs involved, through the imposition and extension of charges — or co-payments — for drugs and certain kinds of treatment. In Germany, for example, charges have been raised significantly in order to avoid increases in social contributions and have been explicitly linked to the latter in an attempt to persuade the insurance funds to keep contributions down, increase efficiency and negotiate more effectively with service providers (GPs and hospitals) over terms.

The success of such a policy, as indeed of the introduction of market, or pseudo-market, mechanisms in countries, depends, in part, on there being effective competition between insurance funds, in the German case, or doctors in countries with national health systems, and consumers being able to choose between them, otherwise prices cannot serve their intended purpose. It is also desirable for there to be competition between service providers to increase the bargaining power of purchasers and to stimulate increases in efficiency. In practice, there tend to be natural limits on competition in both areas, because of the localised nature of supply and economies of scale, which are often reinforced by government to avoid, for example, the closure of local treatment centres.

Accordingly, attempts to introduce market mechanisms have not, in general, led to the increases in efficiency expected, and governments throughout the Union have been reluctant to relinquish controls on expenditure and leave this to market forces. Nevertheless, in countries where an attempt has been made, there appear to have been some gains, without any noticeable deterioration in service. These have arisen from the clearer division between purchasers and providers, the greater weight given to costs in decision-making, the collection and provision of more information on costs and the drawing up of more detailed contracts on service supply.

In the UK, for example, indicators show a small rise in productivity since reforms were introduced in 1991. In Italy and Spain, the separation of purchasers from providers and, in the former, the devolution of financial as well as organisational responsibility to the regions, seems to have led to improvements in management and clearer contractual arrangements between the two sides. In the Netherlands, the recent introduction of a system of *per capita* payments to insurance funds based on a prior assessment of the costs implied by their membership structure, in place of one where effectively costs were covered *ex post*, has led to competition over fees and pressure to contain costs and might, in turn, with partial removal of controls, lead to increased competition between providers and efficiency improvements in this area.

At the same time, the innovatory step has been taken in the Netherlands to confine the public health service to the provision of 'curative basic health care' (as well as of long-term care), and to leave other treatment ('amenity care') to the private sector and individual arrangements. The criteria used to define the latter — that it should not be medically necessary and be affordable — has, however, led to problems in practical application (not least because of the inevitably subjective nature of the concepts used) and so far very few services are excluded from the public sector.

Providing long-term care

An estimated 10% of people aged 75 and over in the Union are in need of full-time care while another 25% require part-time care. The present high growth of population in this age group is focusing increasing attention in Member States on how this expanding need should be met — whether through the social protection system, and if so, whether through transfers or the direct provision of services, either way implying increased taxes and/or social charges, or through private arrangements, implying the acceptance of an unequal burden falling on different individuals, whether they take out private insurance cover or not.

Debate has been partly prompted by the introduction in Germany in 1995 of a new social insurance scheme for long-term care (*Pflegeversicherung*), funded by social contributions (compensated by the loss of a day's holiday) and payable to both those being cared for at home and those receiving residential care. Allowances for carers are of longer-standing in the UK and Ireland, though in the former, they are payable at a relatively low flat-rate and apply only to those providing care virtually full-time, and in the latter, they are means-tested. In Austria, attendance allowances (*Bundespflegegeld*), administered by the regions but funded from general taxation, have been payable since 1993 to people needing care for at least 50 hours a month, at rates varying according to the amount of care medically assessed to be required.

Those receiving allowances in Austria are free to decide how to spend them (most going to informal care within the family). Rising unemployment, however, has led to calls for payments to be linked with employment objectives and used directly to create demand for formal social services. This is, in essence, the option chosen in the Nordic countries, where there is little distinction between health care and social services, both being freely available to all, and where, in relation to working-age population, these account for substantially more jobs than in the rest of Europe (over twice as many in Denmark and Sweden). Nevertheless, budget constraints have led to cutbacks in expenditure and growing concern about the costs of maintaining extensive social services.

Elsewhere, a draft bill was published in Luxembourg in 1996 for the introduction of a compulsory 'dependence insurance' scheme to cover assistance required by those unable to take care of themselves, the funding divided evenly between social contributions and general taxation.

Targeting expenditure

The twin concern of present policy on social protection across the Union, to contain costs and reduce dependency, is being achieved in part by increasing the effectiveness of expenditure through the adoption of a more active approach and targeting resources on those most in need. In Southern Member States, this is combined with efforts to rectify gaps in the protection provided and to balance the provision of support more equitably. In Northern Member States, debate is centred on the scope of social protection. While the consensus on maintaining the universal nature of social protection accessible to all holds firm, this does not rule out some shift in responsibility from the state to the individual or the private sector in certain areas.

Privatisation, however, in the sense of the private, profit-making, sector being involved in providing social protection has not developed very far in most countries and there is little sign, outside of the provision of supplementary pensions, of any significant growth in the foreseeable future. Nevertheless, there is evidence of increased concentration of expenditure on those in need, both through reducing benefits going to those on relatively high incomes, by setting a ceiling on the amount payable or imposing taxes and/or social charges on benefits, and through greater recourse to means-testing. The former serves not only to redistribute the net gain from transfers from the more wealthy to those further down the income scale but also to spread the cost of financing more widely, an increasingly justifiable aim given the growth in wealth of many pensioners.

Although spending on benefits subject to means-testing has generally increased in the Union (apart from in the Netherlands), it still accounted for only 11% of the total in 1995 as against 10% in 1990, and only in Ireland (where it was 34% of the total), the UK (23%) and Spain ($13^1/_2$%) was it more than 10%. Moreover, much of the rise was due to changes in underlying circumstances — in the growth of long-term unemployment, for example, and in the number of people not eligible for social insurance benefits — rather than a change in policy as such. In the case of unemployment compensation, almost 75% of transfers in Ireland were means-tested in 1995 (reflecting high levels of youth and long-term unemployment), 50% in the UK, 40% in the Netherlands and around 25% in Spain and Portugal.

Chapter 1 Social and economic trends

Despite the unprecedented levels of economic prosperity in the European Union, the demands imposed on systems of social protection are probably greater now than they ever have been. At the same time, the nature of those demands have changed significantly over time as the structure of both the economy and society has altered. The aim of this chapter is to describe and quantify the main developments which have occurred over the past decade or so and the trends which seem set to continue into the future. These determine the context in which social protection systems have to operate and are key elements in the debate on reform which is now taking place. As such, it is intended to serve as background analysis to the remainder of this report which is focused on the debate and policy developments across the Union.

Three broad aspects of the change in underlying circumstances which are common to most Member States are examined here in particular. (It should be emphasised that the aim is not to cover all developments with implications for systems of social protection but simply to document a number of ongoing trends which are having a major effect.) The first are demographic trends which are altering the age structure of the population dramatically and which will result in a sharp increase in the number of people above pensionable age in the Union in 10–15 years time. The second are economic developments in the form specifically of high levels of unemployment and increasing participation of women in the work force. The third are changes in the structure of households associated with the decline in the importance of the traditional family and with the growth in the number of people living alone. These developments have tended to reinforce each other in adding to the demands on systems of social support. At the same time, they have occurred in a context where employment has become less secure, as reflected not only in high unemployment, but in the growth of part-time and temporary work.

Demographic trends

The population above retirement age imposes disproportionate demands on social protection, in the form not only of old-age pensions, which are the largest item in social welfare budgets across the Union, but also of health care, a major part of expenditure on which is devoted to the elderly. The ageing of the population has been a feature of demographic developments in most Member States in recent years and is set to be even more important in the coming decades.

In all Member States, as a consequence of declining birth rates and falling death rates, population below working age (under 15) is declining, while that above working age (65 and over) is increasing. In the Union as whole, the number of young people under 15 declined from 19½% of total population in 1985 to 17½% in 1995 and, on the latest Eurostat projections, is expected to fall further to 16% in 2010 and to only 15% in 2020 (Graph 7). By contrast, those of 65 and over have increased from 13% of total population in 1985 to almost 15½% in 1995 and are projected to rise to 18% in 2010 and 20% in 2020. At the same time, the proportion of people of working-age, who are primarily responsible for generating the income to support both young and old, which rose slightly over the 10 years 1985 to 1995, will begin to decline in future years, at first marginally and then more significantly from 67% in 1995 to 64½% in 2020. This implies sharply increasing dependency rates as described below.

The age structure of the population in 1995 was much the same in most Member States, those under 15 accounting for 16 to 19% of total population in all except Italy, where the proportion was only 15% and Ireland, where it was almost 25%. The share of those of 65 and over was generally around 15 to 16%, though it was only 13% in the Netherlands and 11½% in Ireland and as high as 18% in Sweden, where working-age population represented only 64½% of the total as compared with 66 to 68% in most other countries.

A shift in age structure from young to old occurred throughout the Union between 1985 and 1995, the decline in the relative number of under 15s being especially pronounced in the Southern Member States and Ireland, in each of which it fell by between 4 and 6 percentage points (most markedly, from 23% to 17% of the total in Spain).

The ageing of the population is projected to continue in all Member States over the medium and longer-term. By 2020, those of 65 and over are expected to account for 19% or more of total population in all countries, except Luxembourg and Portugal (18%) and Ireland (16%), and for as much as 22% in Finland and 23% in Italy. The increase is likely to be most marked in the latter countries together with the Netherlands, the share rising by 6 percentage points, though it is also expected to exceed 5 percentage points in Germany, France and Greece.

Moreover, the average age of those of 65 and over is also set to increase significantly in the coming years, so putting even greater pressure on health and social services, the demand for which tends to rise dramatically as the elderly grow older. Estimates suggest, for example, that the average cost of providing health care to someone aged 65–74 is, on average, 2–2½ times higher than for people under 65 and for someone of 75 or over, 4–5 times higher. The demand for social services is likely to show even larger differences, though no estimates are available. In 1995, 41% of people aged 65 and over in the Union were 75 or over. By 2005, this is projected to increase to 45½% and in 2010 to 47%, an increase of 37% in numbers in just 15 years (an average growth of over 2% a year). Although total population in the Union is likely to increase by only 3% over this period, therefore, the 'healthcare-adjusted' rise (ie the rise calculated by weighting people of different age by the relative cost imposed on health services) is almost 10%. Beyond 2010, though total population is unlikely to change much, the number aged 65 and over is projected to continue increasing, as noted above, implying a health-adjusted growth in population of around ½% a year.

The projected growth in the number of people of 75 and over, however, varies considerably between Member States. In 5 countries — Greece, Spain, France, Italy and Luxembourg — it is expected to be more than 50% in the 15 years 1995 to 2010 (in Greece, almost 60%), adding strongly to demands for health care and social support, whereas in Sweden, it is forecast to be only 6% and in Denmark, only 2%. In the following 10 years, growth is projected to slow down in most Member States, though still to be significant, but to accelerate in the latter two countries and in Germany, where over the 25 years 1995 to 2020, those of 75 and over are likely to increase by almost 75% (well over 2% a year).

Dependency rates

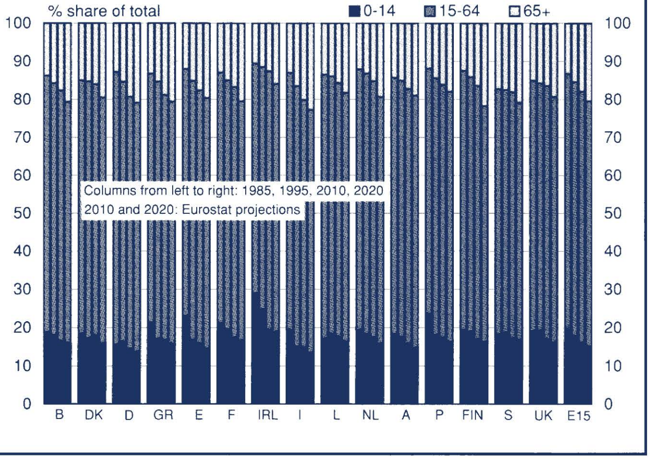
The relative changes in the population of 65 and over and in people of working age which are in prospect have important implications for dependency rates, or, in other words, the number in the former age group relative to the latter, members of which, as noted above, will for the most part need to generate the income required to fund the social transfers and support for those in retirement. Dependency rates have changed only slowly in the past, except in a few Member States. In 1970, for example, the population aged 65 and over in the Union amounted to 18½% of the population of working age. In 1980, the figure had risen to 20% and in 1995 to 23% (Graph 8). In other words, on average, there were less than 4½ people of working age to every one person aged 65 and over in 1995, as against over 5 people for every one of the latter 25 years earlier. In Ireland, Austria and Sweden, moreover, the latter ratio rose slightly rather than falling over this period, while in France, Luxembourg and the Netherlands, there was very little change.

By 2010, those of 65 and over in the Union as a whole are projected to be 27% as numerous as those of working age and by 2020 almost 32%. Instead of 4½ people of working age to every one of 65 and over as at present, therefore, there will be only just over three. The forecast rise in dependency is particularly large in France, where those of 65 and over will increase from 23% of working-age population to almost 33% over the next 25 years, the Netherlands, where the figure will go up from 19% to 30%, Italy, where the increase is from 24% to 35½% and, most remarkably, Finland, where it is from 21% to 35%. As a result of these increases, by 2020, there will be less than three people of of working age for every one person of 65 and over in Italy and Finland and the ratio will be significantly more than three to one only in Austria, Luxembourg and Portugal (around $3^1/_2$ to one) and Ireland (four to one).

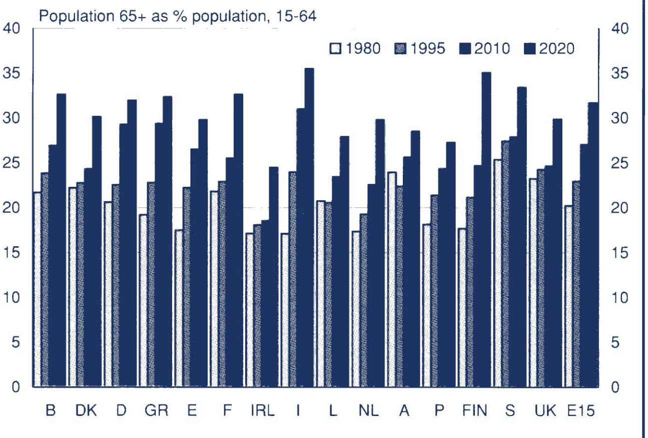
However, while the dependency rate as measured above is a useful indicator of the potential increase in the financial cost of providing social support for the elderly falling on the population of working age, it does not take account of the proportion of those in the latter age group who are actually in work and, therefore, contributing to the output and income in the economy from which the funding for support has to come. This, in practice, varies significantly across the Union, even as between countries where the age structure is similar, not only because of varying rates of unemployment but, equally importantly, because of varying rates of labour force participation, especially of women, as noted below. Accordingly, the effective dependency rate is higher than the 'hypothetical' one described above and differs much more as between Member States.

In 1995, the effective dependency rate was just under 39% (the number of those of 65 and over amounted to 39% of those in employment), implying that there were only just over $2^1/_2$ people in paid work for every person of 65 and over (Graph 9). Only in Denmark, Luxembourg and the Netherlands was the ratio much lower than this — less than three to one (around 30% in the graph, in the first, largely because of a high employment rate; in the second, largely because of a high non-resident work force, which effectively provides a substantial part of the fin-

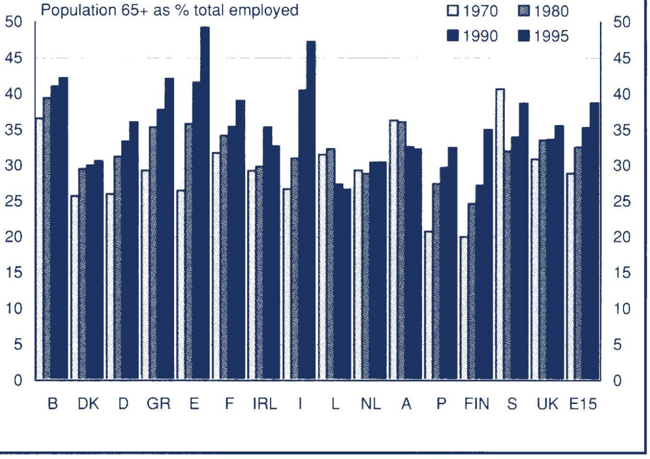
7 Population distribution by broad age group, 1985, 1995, 2010 and 2020



8 Hypothetical dependency rates in Member States, 1980, 1995, 2010 and 2020



9 Effective dependency rates in Member States, 1970, 1980, 1990 and 1995



ance for social protection; and in the third, largely because of a low ratio of people of 65 and over to working-age population — it should be noted that a high proportion of those in work in the Netherlands were employed part-time, which distorts the comparison a little). By contrast, there were less than $2^1/_2$ people employed for each person of 65 and over in Belgium and Greece (because of low employment rates) and only just over two for everyone of 65 and over in Spain and Italy (in both, because of low employment rates, in Italy, combined with an unfavourable age structure).

Effective dependency rates in most Member States have risen much more markedly than the hypothetical ones examined above over the past 25 years. In the Union as a whole, the number of people of 65 and over in 1970 amounted to 29% of employed population, almost 10 percentage points lower than in 1995, which represents a rise of a third over the period, the increase being as much the result of a reduction in the proportion of working-age population in work as of demographic trends. The increase was particularly large in Spain and Italy — over 20 percentage points — in both of which there are relatively high levels of unemployment combined with low rates of labour force participation, primarily because of comparatively few women working and increasing numbers of people retiring early. In stark contrast, the effective dependency rate fell over the 25 years in Luxembourg, Austria and Sweden, though in the last, it has risen appreciably since 1980 and even more since 1990, when unemployment has increased sharply.

These developments demonstrate the importance of taking account of the number of people in work as well as the age structure of the population when assessing the implications of future demographic changes and the growth in the number of elderly people, in particular. They indicate, for example, that to keep the effective dependency rate from rising by more than 10 percentage points over the next 25 years would require an increase in the employment rate in the Union (the number employed relative to working-age population) from 60% to 65%. This is a relatively modest target by international standards (in both the US and Japan, the employment rate is almost 75%), but it would mean restoring employment to the level it was 25 years ago before the slowdown in economic growth and the rise in unemployment. On the other hand, if the low growth and poor job creation performance were to continue, the rise in the effective dependency ratio could be even larger than implied by demographic trends and the implicit problem of providing social support for the elderly even greater.

The main conclusions to be drawn from this are that:

- future employment developments are at least as important as demographic trends;
- favourable developments in employment could offset much of the consequences of the rise in the dependency rate in the coming years;
- by implication, the trend towards early retirement, which has contributed to the rise in effective dependency, needs to be reversed if the employment rate is to be increased, especially given the potential importance of growing numbers of young people remaining longer in education and initial vocational training to ensure that labour force skills keep up with the needs of the economy (the growth in early retirement is examined in Chapter 5).

Changes in the structure of households

The ageing of the population in the Union, described above, is taking place at the same time as support for the elderly from within the family is becoming more difficult, as the extended family declines in importance, households become smaller, families more dispersed geographically and more women, still the main carers, pursue working careers. The consequence is a growing demand for support services and, in some cases, social transfers. Indeed, there is an interactive relationship between the structure of households and systems of social protection, in the sense that just as changes in the former have implications for the latter, the support available from the latter can either facilitate changes or exercise an important constraint on them occurring.

The trend towards smaller households — and accordingly an increase in the number of households — can be illustrated by changes over the 10 years 1986 to 1996 (as indicated by data from the Community Labour Force Survey, which is household-based). Over this period, the average number of people of 15 and over per household declined from 2.15 to 2.05, a fall of around 5% (Graph 10). (The Union here excludes Denmark and Sweden, for which no consistent data are available, though this is likely to affect the figures only marginally.) Given the growth of population in this age group, this implies a growth of around 1% a year in the number of households in the Union, twice the rate of population increase.

The decline in household size was common to all Member States except Italy, where there was a small increase from a figure already above the Union average. The largest fall occurred in the UK and the Netherlands (around 8% in each case), and the extent of the decline was generally greater in the North of the Union than in the South (in Portugal and Spain, the fall was less than 2%). Accordingly, the difference between average household size between the Northern and Southern Member States widened over this period, so that in 1996, whereas the number of people of 15 and over per household was 2.3 or above in all of the latter (and as high as 2.7 in Spain), in most of the North, it was below 2 (and as low as 1.7 in Finland).

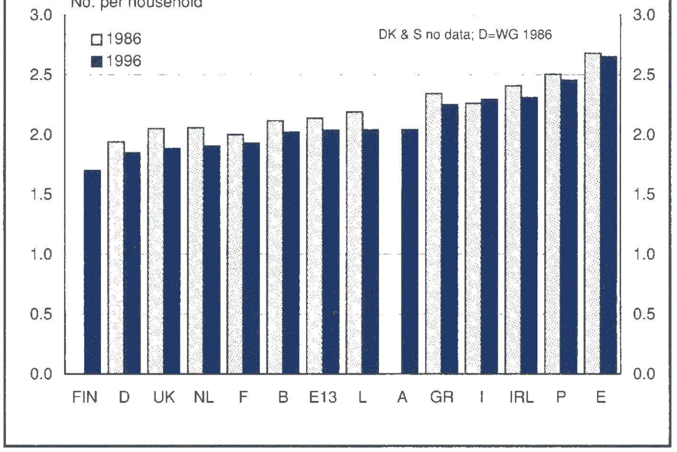
The reduction in household size has been associated, in particular, with a growth in the number of people of working age living alone (ie leaving aside the high proportion of those of 65 and over who also live alone). Over the 10 years 1986 to 1996, one-person households increased from 19% of the total number of households to 24% (households are here defined to include only those in which someone aged 15 to 64 is living so as to focus on working-age population). The rise was common to all Member States, but was especially pronounced in Belgium, Ireland and, most especially, in the UK, where the share increased from 17% to 28% over the period (Graph 11).

Despite the significant growth in share in three of the four Southern Member States — all except Italy — where the relative number went up in each case by over 20%, the proportion of households consisting of someone living alone is much less (under 15% of the total in 1996) in the South of the Union than in the North, Ireland apart, where the figure is over 30% in Germany and almost 40% in Finland.

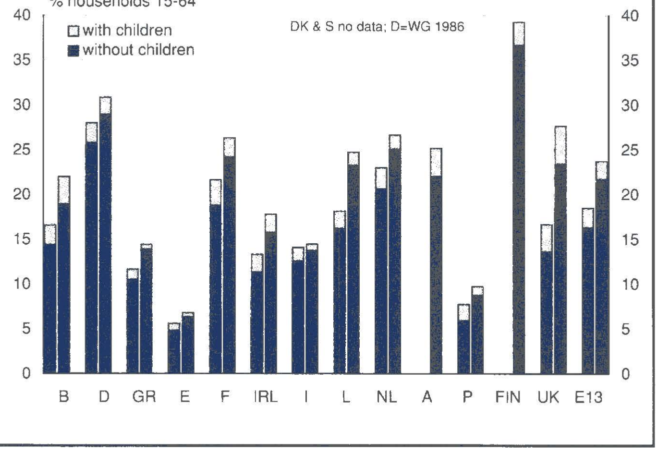
The number of one-person households with children increased even more markedly, by some 64% between 1986 and 1996 (an average of 5% a year), though in relation to the total number of households, it is still comparatively small (just over 3% in 1996, 14% of all lone 'working-age' person households). Growth occurred in all Member States, except Italy, where there was a slight fall, though the rise was relatively small in Greece and Portugal (under 10%). In the UK, the increase was dramatic (averaging 10% a year over the period), and in 1996 lone parent households accounted for almost 7% of all households (25% of one-person households), much more than in any other Member State.

The overwhelming majority of lone parents with children throughout the Union are women, women account-

10 Average number of people aged 15 and over per household in Member States, 1986 and 1996



11 Share of households with only one person aged 15 and over in Member States, 1986 and 1996



ing for around 90% of the total in all Member States, and as much as 95% in Austria, with only Italy having a figure below 85%, and then only marginally (Graph 12). Moreover, their share increased in most countries between 1986 and 1996, when just under a quarter of all working-age women living alone in the Union had children, though only 11% in Greece and around 16% in Germany, Italy, the Netherlands and Luxembourg, but a third in Ireland and 40% in the UK.

Workless households

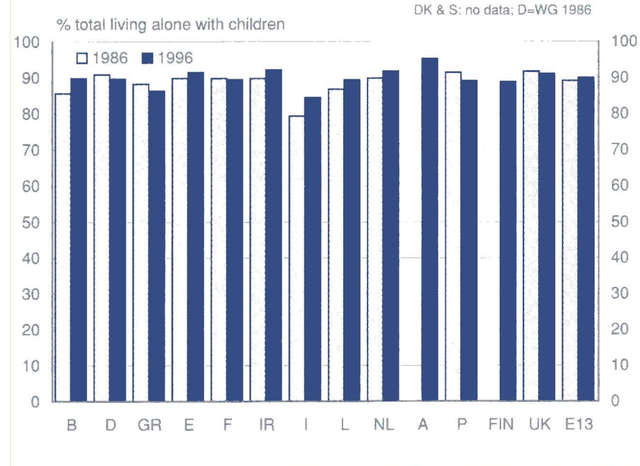
The social protection implications of the growth of one-person households are given added significance by the fact that people living alone are more likely to be unemployed than those living with other people. This, at least, is true of men and of the North of the Union rather than the South. In the Union as a whole, around 16% of men aged 15 to 64 who were unemployed in 1995 lived alone (or, more precisely, in households with no other person of working age) as compared with 11% of men in employment. This disparity, however, was confined to the North of the Union, whereas in the South, men living alone were more likely to be in work than unemployed. In Finland, the Netherlands and Germany, 25% or more of men unemployed lived alone and in Belgium and the UK, over 20%, in the latter four cases, around twice the proportion of those in employment living alone (Graph 13).

In Greece, Italy and Spain, on the other hand, proportionately fewer of the men unemployed lived alone than those with jobs, and the relative numbers involved were small ($4^1/_2$% in Greece, 4% in Italy and 2% in Spain), as was also the case in Portugal (3%), where there was comparatively little difference between the proportion of men unemployed living alone and those in work.

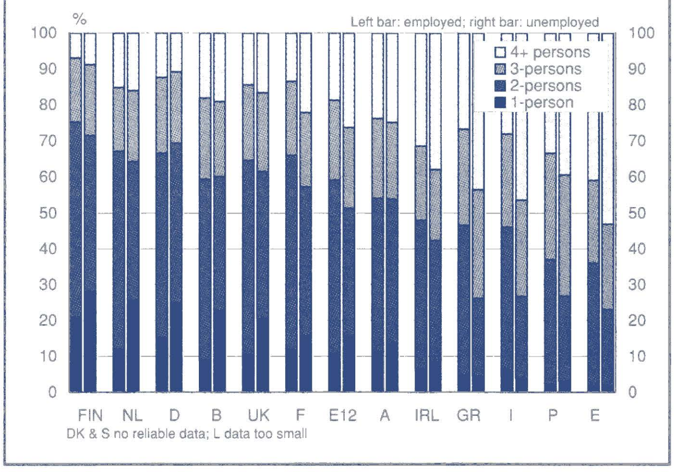
For women, the difference between the household characteristics of the employed and unemployed is much less pronounced than for men, at least at the Union level, much the same proportion in 1996 living in households where they were the only person of working age. The same kind of difference, however, is evident between the North and the South of the Union as for men. In all Northern Member States, the proportion of women who were unemployed and living alone was higher or the same (France) as that for women in work — the difference being especially marked in Finland, the Netherlands, Belgium, the UK and Austria, where in each case, as for men, some 20% or more of women unemployed lived alone (Graph 14). In three of the four Southern Member States, by contrast, proportionately fewer women unemployed lived alone than those with jobs, and in the fourth, Portugal, the proportion was much the same.

The sharp distinction between the North and the South of the Union in this regard emphasises the equally large differences in the support implications of unemployment between the two. In Southern Member States, virtually all the men and women who are out of work live in households with other people of working age, who can potentially provide financial

12 Lone mothers with children in Member States, 1986 and 1996



13 Employed and unemployed men, 15-64, by size of household in Member States, 1996



support. Many of them, in practice, are young people under 25 living with their parents. In Northern Member States, on the other hand, significant numbers of the unemployed of both sexes live in households with no other person of working age and, accordingly, are dependent on financial support from outside. Though support may come from other members of the family living elsewhere, the implication is that there is a greater need for income support from the State in these countries than in the South of the Union.

At the same time, the nature of social protection systems in most Northern Member States means that people are more able to live alone if they are unemployed than in the South. Young people under 25, for example, have no entitlement to unemployment benefit or social assistance in Greece and Portugal if they are not working and in Spain and Italy, comparatively few are likely to be eligible for support. In the North of the Union, there is generally more entitlement to social support for people in this age group, though, perhaps relevantly, less in France, where relatively few of the unemployed live alone, than elsewhere.

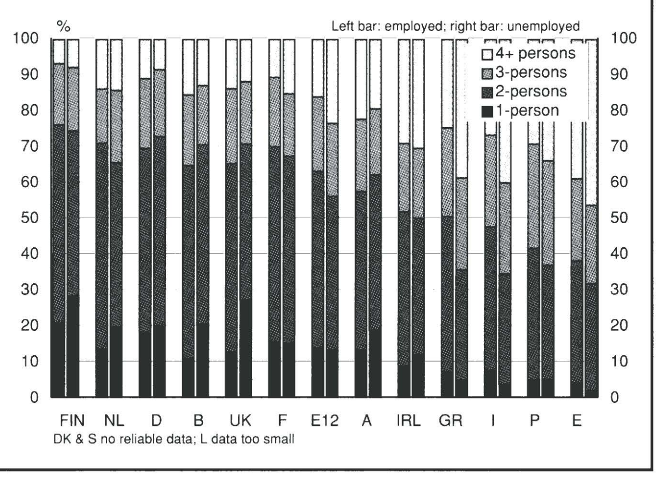
It is also significant as regards support that the great majority of the unemployed in Southern Member States live in households where there are three or more people of working age (around 75% of men and two-thirds of women) and a large proportion in households with four or more (40% or over), significantly more in each case than for those with jobs. By contrast, in the North of the Union, with the exception of Ireland, a minority of the unemployed lived in households with three of more people.

The increase in the relative number of people living alone is a major factor underlying the growth of households with no-one in work which has occurred over the past decade, over and above the rise in unemployment itself. Indeed, the widening division in European societies between 'workless' households and those in which everyone of working age is employed is a marked feature of recent developments right across the Union, even in the Southern Member States where comparatively few people live alone.

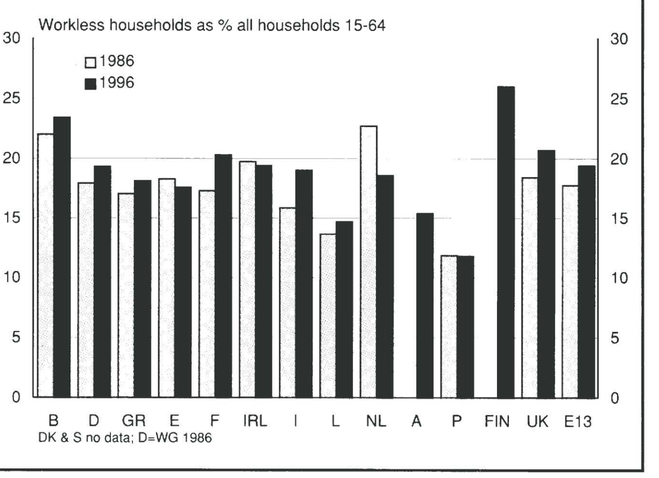
In 1996, just under 20% of households containing at least one person of working age had no-one in work, either because they were unemployed or economically inactive. This compares with a figure of 18% in 1986 (Graph 15). Although the rate of unemployment also increased over these 10 years, the rise (from 10.3% to 10.7% for the 11 Member States for which comparable household data exist for the two years) was less than in that of workless households.

The variation in the relative number of workless households between Member States, moreover, was relatively small, far less than the variation in unemployment rates. Whereas the latter varied from over 22% in Spain and 15½% in Finland to only 4% in Austria and 3% in Luxembourg in 1996, the proportion of workless households with someone of working age ranged from 26%

14 Employed and unemployed women, 15-64, by size of household in Member States, 1996



15 Share of households with nobody in employment in Member States, 1986 and 1996



in Finland to 12% in Portugal, which was the only country where the figure was below 15%. Even in Austria and Luxembourg, where unemployment was low, around 15% of households containing someone of working age had no-one with a job.

In most Member States, the relative number of workless households increased between 1986 and 1996, the rise being particularly marked in Italy and France (3 percentage points in both cases), as might be expected given the rise in unemployment (by over 2% of the labour force in both cases) (Graph 16). However, the proportion of workless households also increased significantly in the UK (from 18½% to 21%) and here unemployment fell even more significantly (from 11½% to just over 8%) and the proportion also rose in Belgium (from 22% to 23½%), where unemployment declined as well, though only slightly, while in Ireland, where unemployment fell by more than in the UK (by 4½% of the labour force), it remained much the same. In these countries, therefore, apparent improvements in the job market have not been accompanied by any reduction in households containing someone of working age with no-one in paid employment and, indeed, in Belgium and the UK, the relative number has risen. Accordingly, the potential need for social support, may also have increased rather than diminished over this period, contrary to the implications of the change in unemployment.

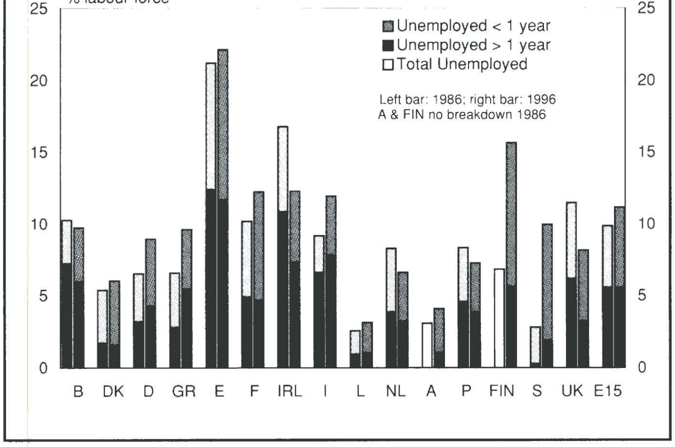
Unemployment developments

Unemployment has remained stubbornly high in most parts of the Union over the past decade, after rising markedly over the preceding decade following the world oil crisis in 1973–74. In 1996, the average rate in the Union was just under 11% of the work force, slightly higher than it was 10 years earlier at its peak after the recession of the early 1980s and only marginally below its level in 1994 after the recession of the early 1990s. The rate was 12% or over in five Member States, including France and Italy, and close to 10% in another three. Moreover, in only three countries, Ireland, the Netherlands and the UK, was the rate significantly lower (over 1% of the labour force) than 10 years before.

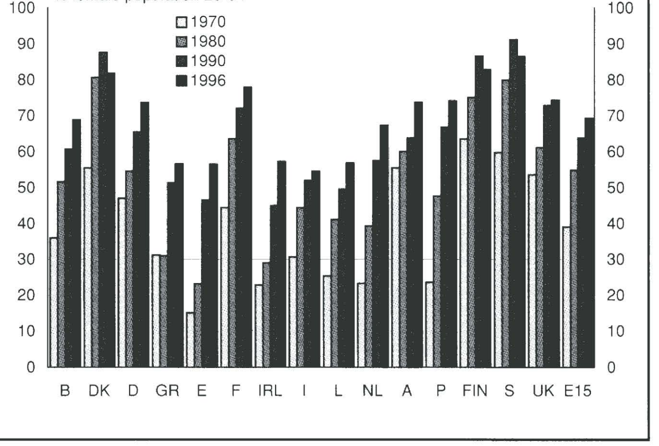
Almost half of those unemployed in the Union in 1996 had been out of work for a year or more, just over 5% of the labour force or nearly 9 million people. Almost 5½ million of these had been out of work for at least two years. Although the rate of long-term unemployment declined between 1986 and 1996, the fall was relatively small. In Belgium and Ireland, it was still the case that around 60% of the unemployed had been jobless for a year or more and in Italy, almost two-thirds (though a high proportion of the latter were young people under 25 and, from the above analysis, for the most part still living with their parents), while in Greece, Spain and Portugal, the figure was well over half.

High levels of unemployment in the Union have been accompanied by the development of more flexible,

16 Unemployment and long-term unemployment in Member States, 1986 and 1996



17 Participation rates of women aged 25-54 in Member States, 1970, 1980, 1990 and 1995



though more precarious, forms of employment. Both part-time and temporary jobs have become more important across the Union, for men as well as women, over the past decade, and in many cases represent the main jobs open to those who are unemployed (see *Employment in Europe, 1997*, Part I, Section 3 for an account of recent developments in respect of the changing nature of employment and Section 1 for more details of unemployment developments).

The growth of women in employment

The increase in the number of women pursuing working careers has been one of the most pronounced features of economic developments in the Union over the post-war years. Much of the increase has occurred over the past three decades when the trend towards women working spread from the North to the South. In 1970, under 40% of women aged 25 to 54 in the Union were economically active, in the sense of either being in employment or actively seeking a job. By 1980, this had increased to 55% and in 1996 to 70% (Graph 17).

Activity rates rose continuously and significantly in all Member States over these 26 years, except in the three Nordic countries, where, partly because of economic recession, rates have fallen in the 1990s from levels which were much higher than anywhere else in the Union (close to 90%, not far below those of men in the same age group). The rise was particularly large in countries where the rate was low at the start of the period — Spain, Ireland, the Netherlands and Portugal. Moreover, except in countries where the rate has reached a relatively high level, there is little sign of the increase slowing down, once allowance is made for the depressed growth of employment during the 1990s (though the UK is a possible exception, the rate showing little tendency to rise from a level only just above the Union average even since the recession of the early 1990s came to end).

As a result, in most Member States (9 of the 15), around 70% or more women aged 25 to 54 are in the work force and only in Italy is the proportion under 55%. The effect of this increase is that most of the new jobs created since 1970 have gone to women and while the number of women in work has risen markedly, the number of men has fallen. A further effect has been to add to the demand for support services in the form of child care facilities and help in caring for the elderly too frail to care for themselves. It has also led to growing calls for equality of treatment of men and women under social protection systems, the individualisation of rights and interruptions to working careers because of caring responsibilities, which still fall predominantly on women rather than men, to be taken into explicit account in the assessment of entitlement to benefit, especially as regards retirement pensions.

Chapter 2 Adapting to change: recent reforms and key developments

As illustrated in the previous chapter, significant social and economic changes are taking place across the European Union. These changes are altering both the context in which systems of social protection operate and the nature and scale of the problems which they have to tackle. In all Member States, the attention of policy-makers has become increasingly focused on the capacity of systems to cater for new needs and to provide adequate levels of support to growing numbers requiring assistance without substantially increasing expenditure, while at the same time shifting to a more active approach of getting people into work rather than merely supporting their income.

The common objective is to maintain the universal social safety net which is a distinguishing feature of European models of society rather than to dismantle the systems developed, often over many decades (though much more recently in Southern European countries where some parts of the net are still in the process of being constructed). At the same time, a number of aspects of prevailing arrangements are being questioned, especially those which have resulted in large numbers being dependent on state support on a seemingly permanent basis and effectively excluded from society. A key aim is to ensure that the support provided is affordable, in the sense of being accepted by the people who have to fund it, and that it supports rather than impedes economic growth and job creation, on which the well-being of society ultimately depends.

These twin objectives have been increasingly difficult to achieve in recent years. Economic growth has been depressed (averaging only $1^1/_2$% a year between 1990 and 1997 over the Union as a whole), so limiting the finance available for social protection. Moreover, there has been increasing concern about budget deficits and a common desire to avoid any significant expansion of public expenditure or increases in tax or social contribution rates, in the short-term to comply with the Maastricht criteria for membership of monetary union and in the longer-term to help create the conditions for sustained, non-inflationary growth.

Throughout the Union, the growing numbers in need of support coupled with tightening constraints on available resources are prompting changes in social welfare arrangements, in the scale of protection provided, the people covered and nature of the measures adopted. At the same time, the substantial increase in the number of people of pensionable age, which is now clearly in prospect in 10 to 15 years time as the post-war baby-boom generation grows older, is reinforcing the pressure for change.

This pressure extends to the provision of social services and health care, for which the growing needs implied by an increasing number of very elderly people add to the seemingly limitless growth of demand emanating from the rest of the population, stimulated by advances in know-how and the treatments available. For pensions, health care and more general care of the elderly, the key issue concerns the extent of protection which the State should provide, whether, at one extreme, there should be universal coverage for everyone or whether, at the other, it should be limited to basic needs only, leaving individuals to secure protection against additional needs themselves through private insurance.

For other areas of social protection, the focus of policy is increasingly on reducing the number of people of working age dependent on long-term support, which insurance-based systems, developed on the principle of contributions being paid when in work to finance temporary spells when not, were never designed to cater for. The objective is to secure ways of getting such people into work. This has led, in turn, to two parallel developments: an attempt, on the one hand, to shift expenditure from passive measures of income support to an active policy aimed at increasing employability and helping with job search and, on the other, to ensure that there are sufficient incentives for people to seek to move from reliance on social transfers into employment.

Although it is difficult to argue that high levels of benefit in relation to potential earnings from work are a primary cause of the high rates of unemployment in the Union — or more precisely of the large numbers out of work and living on income support — they might potentially conflict with active measures being taken to get them into employment. More importantly perhaps, in a context of resource constraints, reductions in spending on benefits may be a condition for increases in active expenditure. Moreover, the maintenance of social solidarity and the continued willingness of people to pay the taxes and contributions required to fund social transfers may well be more difficult to secure if benefits are regarded as overly generous, especially during periods of low income growth. The need to maintain popular support for systems of social welfare together with budget constraints, has led, in addition, to greater efforts to combat fraud and abuse and to tighten up eligibility criteria so as to demonstrate that those in receipt of transfers are deserving cases.

While the developments described above and in the previous chapter have been common to all Member States, their scale has varied significantly. This has affected the strength of the pressure for change to systems of social protection, as have differences in their structure (see *Social Protection in Europe, 1995*, Chapter 1, for a description of the different systems in operation), the effectiveness of the arrangements in force and extent of popular acceptance of them. These differences mean that, while there are common elements, the scale and the precise detail of the problems facing social protection systems are by no means uniform across the Union. The changes in policy which have taken place or which are being actively discussed reflect such differences.

For example, while inadequate rates of employment growth have prompted growing policy concern in most parts of the Union about the way in which social protection systems are financed, this has especially been so in countries where the insurance principle predominates and finance comes mainly from contributions levied on earnings from employment (the mainland Member States, excluding the three Nordic countries). In these countries, there has been a common effort to limit the charge falling on employers, to lower the cost of employment and so stimulate increased job creation. The focus, in particular, has been on low-paid, and less-skilled, workers, especially the young and the long-term unemployed, for whom the imposition of a social charge is liable to make it unprofitable for employers to take them on.

In addition, in Southern European Member States, where universal systems of social protection are of more recent origin, the concern remains to fill the gaps in protection — in guaranteeing a minimum level of income, for example — and to provide more standardised coverage for people in different regions or in different occupations (to rationalise the highly fragmented nature of pension schemes, unemployment insurance and health care provision, in particular). Reformers, however, face the same kind of budgetary constraints as in the rest of the Union and the same kind of economic and demographic pressure for expenditure increases, making it even more difficult to achieve these objectives, while they also have to contend with the vested interests which the existing fragmented system has created.

Outline

The concern here is to review the changes in systems of social protection which have taken place over the past few years or which are in prospect, focusing mainly on the period since 1995 (for changes before then, see *Social Protection in Europe, 1995*, Chapter 2). The aim is not to present an exhaustive list of such changes (for this, see the *MISSOC*. reports for 1996 and 1997 which set out in detail the measures which have been introduced in each Member State), but to concentrate on those which seem most significant and to analyse the motivation behind them and their potential effects.

The analysis is divided by theme rather than function. Specifically, it examines, first, the changes made in relation to those of working-age who are not in work, whether they are actively seeking employment (and, therefore, counted as unemployed) or not. Such changes have been a prominent part of the policy followed by Member States in recent years. They have taken two main forms: a reduction in the effective level of income support in relation to earnings when in work, aimed at reducing social expenditure and increasing the financial incentive to find a job, and a shift in emphasis towards active measures to increase employability and get as many people as possible into work.

Secondly, it considers the changing policy stance towards older workers, from encouraging them to withdraw from the labour force before the official age of retirement, in order to free up jobs for others, to increasing the financial incentives for them to remain in work.

Thirdly, it reviews the response by Member States to the prospective increase in the number of retirement pensioners in future years and the substantial growth of transfers which this is liable to entail.

Fourthly, it examines the changes to systems of health care introduced in an attempt to contain costs, while maintaining or improving levels of service and access for all, a potential conflict in objectives which is likely to become more acute with the ageing of the population.

Fifthly, it summarises the measures being taken in the face of the growing need for long-term care implied by the significant increase in the number of people living into very old age.

Sixthly, it examines attempts in Member States to distribute the cost of financing social expenditure more widely across society and, in particular, to reduce social charges levied on employers which could deter job creation.

Finally, it considers how far the scope of social protection systems is changing in response to the common objective of reducing dependency in the context of cost pressures stemming from budget constraints.

Reducing the cost of unemployment

The persistence of high rates of unemployment in most parts of the Union and, in particular, of the substantial number of long-term unemployed, has focused increasing attention on ways of reducing the cost involved. In a number of Member States, the regulations governing entitlement to unemployment insurance benefit have been tightened in the past few years and/or the definition of what constitutes a suitable offer of employment widened. In the Netherlands and Sweden, for example, the qualifying conditions for unemployment benefit were made more stringent in 1993, while in Spain in the same year, the prior contributions record required for eligibility for benefits was lengthened, as it was in Austria in 1995 (young people and those unemployed before needing to have been employed for at least 6 months to be entitled at all) and in Finland in 1997 (from 6 to 10 months).

Rates of benefit have also been reduced. In Germany, both the insurance rate and the rate of means-tested social assistance (which benefit recipients have to fall back on after being unemployed for a year) were reduced in 1994, while in Finland, the real value of benefits has been reduced by their non-indexation in 1995 and 1996. In Sweden, by contrast, the benefit rate was increased from 75% of previous earnings to 80% in 1997.

In addition, the period of entitlement to insurance benefit has been shortened in some Member States. In the UK, the period was reduced from one year to only 6 months on the introduction of the *JobSeeker's Allowance* in 1996, benefit remaining flat-rate rather than being related to previous earnings as in all other Member States except Ireland and set at a lower level than in most other parts of the Union. Thereafter, payment becomes means-tested. In addition, insurance benefits were reduced for people under 25 and housing benefits restricted.

At the other extreme, the benefit period was reduced in Denmark from 9 years before 1995 to 5 years in 1996, though it remains among the longest in the Union. At the same time, for the last 3 years of the period, intensified efforts are made to get the unemployed into active programmes. Moreover, in Belgium, where the period of entitlement to unemployment benefit is also relatively long, authorities were given the power in 1996 to suspend payment if someone has been unemployed for longer than $1^1/_2$ times the regional average instead of twice as long (36,000, many of them married women, lost benefit as a result in 1996, 10,000 more than in 1995).

Increasing the incentives to work

Cuts in benefit and the tightening of eligibility criteria provide in themselves an increased incentive for the unemployed to find a job. Other measures have also been introduced in a number of countries to make it more attractive, and in some cases more feasible, for people to work rather than remain unemployed. Such measures can take various forms, though in essence they involve increasing the take-home pay from employment — after taking account of specific costs, such as providing for child care — relative to net income from benefits. This means ensuring that the combined effect of the tax and benefit systems on the net income of people in different circumstances accords with government objectives regarding work incentives, something which has not always been the case in the past (the two systems often having been developed independently of each other).

Paradoxically, one potential source of difficulty is targeting, or concentrating social transfers on those most in need, a difficulty which has tended to become more prevalent with the growing importance of means-testing (documented below). If benefits are withdrawn once income exceeds a given level — as a person moves from being unemployed to having a job, in particular — then the net gain to being employed can be relatively small, or even in some cases negative. This implies that benefits, such as family allowances, housing benefits or relief from various kinds of charges, which are given in addition to unemployment benefits tend to have less of a disincentive effect if they are universal, in the sense of applying to those in work as well as those who are not, and if they are invariant to income (though this would clearly conflict with other aims). It also illustrates the potential conflict between major objectives of social protection programmes — on the one hand, of eliminating poverty, which is likely to involve increased targeting given funding constraints, and, on the other, of making systems employment-friendly.

In all Member States, except in Spain where there are implicit transfers in the form of tax concessions, benefits are paid to families with children. In most countries, the amount paid is independent of income, though in Germany, Italy and Greece, they are reduced when income exceeds a certain level, so giving rise to possible incentive problems. This has also been the case in Portugal since 1997, when the system of family benefits was reformed and three levels of payment were introduced according to family income (under 1½ times the minimum wage, 1½ to 8 times and over 8 times), and in Greece since 1997, when benefits were increased to families with more than two children but were limited at the same time to families with income of less than a given amount (8 million drachmas a year, or around 25,500 ECU). The effect on incentives is likely to be small in the latter country, where very few households, especially those vulnerable to unemployment, have incomes above the ceiling.

The same applies, though to a much lesser extent, in France, where the new Government has announced its intention of withdrawing child allowances from families whose monthly income is higher than 25,000 francs a month (around 3,800 ECU, which would probably affect some 10% of households according to European Community Household Panel data).

In Ireland, there has also been a substantial increase in family allowances, as in Portugal and Greece, but without any income ceiling being applied to eligibility. Here, as in the other two countries, having children was identified as a major cause of poverty (and the provision of free services and exemption from charges to those dependent on social transfers as a major disincentive to finding employment). Benefits for the first two children were increased by 45% in 1995–96 and for each subsequent child by 36% in order to combat the problem.

Nevertheless, although the practical effect in most instances may be limited at present, the potentially adverse consequences for work incentives of income-related benefits need to be explicitly taken into account when systems are reformed. In general, it argues for a gradual reduction of the various benefits, not just family-related ones, as income increases rather than their abrupt elimination. Such a graduation may be more readily achieved if benefits are subject to tax — or, more precisely, treated as part of income which is subject to tax in the same way as earnings from employment — than if they are not. As noted below, charges on benefit recipients have been increased in a number of countries in recent years, ostensibly to spread the cost of funding social expenditure more equitably across the community.

The potential effect on work incentives also argues for a differential limit to be fixed when there are two (actual or potential) wage-earners in a household, otherwise there may be little incentive for either one of them to work if, for example, the other is unemployed and receiving means-tested benefits or earning a sufficiently low wage to qualify for housing allowances or in-work benefits. Despite the increased relevance, with the spread of targeting, of this possibility, and despite the fact that means-testing is everywhere applied to household rather than individual income, no country has as yet introduced such a differentiated system, nor is there much sign of it being seriously debated.

Indeed, in a few Member States, it remains the case that some benefits — though a declining number — are paid only if the person unemployed lives with a partner who is not in paid employment or works for less than a maximum number of hours a week. This applies, for example, to the payment of additional unemployment benefits in Belgium or to eligibility for means-tested income support in the UK, where partners have to work 24 hours a week or less (though this was increased from 16 hours with the introduction of the *Jobseeker's Allowance* in 1996). Such conditional benefits are an obvious cause of an 'unemployment trap', reinforcing any effect on relative income levels of targeting.

In-work benefits are another means of increasing net income from employment relative to income when unemployed. However, since they are confined to those on low wages — and, indeed, arguably entrench low rates of pay by making the jobs to which they apply more attractive — and involve a very high marginal withdrawal rate as income rises, they are similar to other social transfers in terms of their potential disincentive effect, in this case discouraging those in receipt from trying to improve their employment situation. (Rather than giving rise to an 'unemployment trap' like benefits targeted on the unemployed, they are a potential cause of a 'poverty trap', insofar as it is difficult for recipients to increase their net income significantly because of the high marginal rates of deduction applying to any rise in gross earnings.)

At present, significant in-work benefits exist in only two Member States, the UK (Family Credit, Disability Working Allowance, Housing Benefit and Council Tax Benefit) and, more recently, Ireland (Family Income Supplement). So far, they are payable for the most part only to people with children, though in the UK, a pilot scheme was introduced in 1996 by the previous Government for low-paid workers without children. Whether this will be developed into a general scheme by the new Government is so far unclear, though the intended introduction of a minimum wage — which is an alternative means of securing higher income for those in work and one which does not have social expenditure implications (though it may affect the jobs on offer and so lead to pressure for job subsidies) — may reduce the need for explicit transfers.

In Ireland, the number of people covered by in-work benefits has increased in the recent past as qualifying income levels have been raised. In the UK, a child-care disregard allowance (ie a sum deducted from earnings when determining eligibility for benefit) was introduced in 1994 and increased in 1996 in order to assist low-paid workers with families. Lone parents have been targeted specifically of late in the two countries, with a new one-parent benefit being introduced in Ireland in 1997, under which recipients are allowed to earn up to a certain amount before payment is withdrawn and through more active measures in the UK, as described below. At the same time, the administration of Family Credit in the UK has been speeded up (90% of claims from employees being processed within 5 days rather than 13) to ensure that those moving into low-paid jobs get this sooner rather than later. In addition, entitlement to housing benefit and relief from Council (local) Tax has been extended to the first four weeks of employment and priority given to sorting out new housing benefit entitlement in order to reduce both the cost and uncertainty attached to the transition.

In a number of Member States — Belgium, Germany, Finland, Portugal, Ireland and the UK — attempts have also been made in recent years to encourage people to take part-time jobs, in part to encourage the development of such working and so make more jobs available, in part to prepare people better for full-time employment (see Chapter 4 for details).

The 'activation' of policy

The measures discussed above have been accompanied by an intensification of active policies. These have been aimed at increasing the employability of those out of work, helping then find a job, encouraging employers to take on more people and providing work directly. Indeed, in many Member States, the emphasis of policy has shifted in this direction, away from a passive approach to an active one, very much in line with the Commission's recent Communication on *Modernising and Improving Social Protection in the European Union* (COM(97) 102) and the conclusions of the Luxembourg Job Summit. Measures have increasingly been targeted on the unemployed who have most difficulty in finding work, the long-term unemployed and young people in particular, though they have also been extended to people dependent on social transfers, who may not actively be seeking work and so not counted as unemployed, but who, nevertheless, are capable of working — lone parents and those with (less severe) disabilities, for example.

The motivation behind this policy is both to help people to improve their situation, for them to become less dependent and more integrated into society (so combating social exclusion), and to reduce social expenditure. Shifting the emphasis of policy from passive measures of income support to active measures, however, is not so easy, especially during periods of low growth and high unemployment. The need for income support is not reduced in the short-term by a simple desire to spend more on active measures. Increased active expenditure tends to mean an expansion of overall spending whatever the long-term consequences might be on the numbers out of work. This can be difficult to finance when high unemployment is already pushing up outlays on social transfers and may well require a restructuring of the latter. The limited success of governments in shifting the balance of expenditure towards active measures, even in Member States where this is proclaimed policy, is testimony to this (see Chapter 4).

In Germany, for example, Federal Employment Agency revenue for financing active as well as passive labour market measures comes mainly from contributions which are divided equally between employers and employees. The rate of contribution required to meet combined expenditure on both types of measure rose from 4.3% of gross earnings in 1991 to 6.8% in 1993 and though efforts have been made to reduce it since, these have proved only partially successful and it remains at 6.5%. Partly in response to this, calls have intensified to widen the funding base to include, in particular, civil servants and the self-employed as well as other groups who at present do not contribute.

Active measures can either involve more spending (on job placement services, the provision of training, employment subsidies and so on) or less revenue, as tax concessions are given (to fund company-based training, for example) or social charges reduced (to lower the cost of employment in the same way as subsidies). There is little material difference between these alternatives, though operating on the revenue side has the cosmetic advantage of both reducing the apparent tax burden and limiting the increase in public expenditure. Since tax concessions or relief from social charges are often not explicitly costed, however, it makes for difficulty in comparing levels of effort between countries.

In a number of Member States — Denmark, Sweden and the UK, for example — conscious efforts have been made to increase the articulation between the provision of income support and getting the unemployed into work, by giving more individual help to the unemployed both to acquire new skills and to search for a job and to do so at an early stage in their period of unemployment (see Chapter 4 for details of active measures). This contrasts with the traditional approach of leaving the unemployed much to their own devices, of providing income support so that they have time to look for a suitable job and of only taking action when the person has been unemployed for a long time. In effect, it is a response not only to the increased pressure on governments to reduce the number unemployed but also to the evidence that the longer someone has been out of work, the more difficult it is for them to find a job.

Relieving poverty and reducing social exclusion

Increased efforts at getting people into work have not been confined to the unemployed, in the sense of those recorded as actively seeking a job. There has been growing concern about the kind of support provided to those not in the labour force at all. In particular, measures have been introduced aimed at both encouraging and enabling many people registered as having disabilities and lone parents with young children to work. In all Member States, social assistance is available to those unable to work for one reason or another, though in some countries — in the South of the Union, especially, this has traditionally been organised regionally or locally — and a minimum level of income has not been universally guaranteed.

In Portugal, however, a scheme guaranteeing families a sufficient level of income to meet basic needs came into effect in July 1997, while in Italy, the Onofri Report recommended the establishment of a means-tested minimum income scheme, with payments related to family size. In addition, in Spain, where social assistance remains the responsibility of the 17 regional authorities, the automatic revaluation of minimum benefit levels has been introduced, and in Sweden, a national scale of assistance, in place of benefit levels determined by the municipalities responsible for support (though in the context of a national norm), was agreed in 1997 (preceded by much debate about how far payments should vary between different localities).

Both the Portuguese and Italian schemes involve not just the provision of income support but measures to help benefit recipients integrate into society. This is essentially in response to the experience under similar schemes of much longer standing in Northern Member States, where it has been clearly demonstrated that social transfers by themselves are not enough to overcome the problem of deprivation and exclusion from a normal social life which prolonged economic inactivity can create. (In France, for example, in both 1992 and 1996, only a third of those covered by the minimum income scheme aimed at getting people back into work — *Revenu Minimum d'Insertion* — succeeded in finding a job.)

There is, therefore, a general tendency throughout the Union to address the underlying causes of poverty and social exclusion as well as the symptoms and to avoid systems of income support becoming the means for entrenching a permanent division in society between those who contribute to its well-being and those who do not. The aim, in particular, is to help those dependent on social benefits to become self-supporting, or at least to have more control over their lives and to play a more active role in society. This means giving them the opportunity to find a job, which, in turn, means not only helping them increase their employability through education and training, but ensuring that they have a place to live and access to adequate levels of health care and social services, such as child-care facilities for lone parents.

There are many examples of a more active approach being taken to encourage people on social assistance to find employment. In Denmark, for instance, from 1998 on, everyone receiving social transfers will be given the chance to return to education or go on to a training scheme. Moreover, they will be expected to take up such opportunities if they wish to continue receiving income support. In Germany also, increased efforts have been made to get those on social assistance into active labour market programmes, while in the UK, the new Government has announced a 'welfare to work' programme aimed at reducing the number of people reliant on benefits.

In addition to *New Deal* programmes for the young and long-term unemployed and disabled people who want to work, the UK Government is in the process of introducing a package of measures to provide help and advice to lone parents to make the move into work. In Great Britain, the number of lone parents in receipt of Income Support has risen from 320 thousand in 1979 to 1.1 million in 1996. The New Deal for Lone Parents involves the appointment of a personal caseworker who offers help and advice with the search of a job, training needs, benefit advice and child-care information. The service, which is offered on a voluntary basis, is primarily aimed at lone parents whose youngest child is at school but it is also available to lone parents with younger children. Already available in eight areas of the country, the service will be available to all lone parents in receipts of Income Support by October 1998 (see Box). There is no plan in the UK to make it compulsory for lone parents to try to find a job or to go on a training course, though they will be encouraged to do so.

In the Netherlands, more stringent procedures for claiming social assistance have recently been introduced, requiring recipients to be actively seeking work and to accept any suitable offer they receive, except if they are lone parents with a child under 5. In Luxembourg, where assistance guaranteeing a minimum income has been extended to those aged between 25 and 30 (previously it applied to

The 'Welfare to work' policy in the UK

The new Government announced plans soon after taking office for shifting the focus of policy on social security from income support to getting people into work, through the *New Deal*. The object of reform across the system is to reduce poverty and welfare dependency, to promote work incentives and to develop a system that supports work, savings and honesty. As a major part of this is to ensure that people are always better off when working than when out of work and, in particular, to remove the fear that people will not be able to afford to pay their rent (covered by housing benefits when out of work) and travel expenses once they return to work. The specific measures introduced in this regard by the previous Government include:

- the continued payment of housing benefits at the same rate for the first four weeks of employment for those on *Income Support* or *Jobseeker's Allowance* for six months or more;
- the ability to build up a *Back-to-Work* bonus of up to £1,000 (1,500 ECU) for those whose benefit has been reduced by working part-time while receiving *Income Support* or *Jobseeker's Allowance* if they start a full-time job;
- the faster processing of claims for *Family Credit* (in-work benefit) for those starting a new low-paid job (within 5 days for 90% of claims);
- the deduction of a child-care disregard from earnings when assessing entitlement to in-work benefits (90 ECU and from Summer 1998, 150 ECU for two children).

The present Government has introduced further measures, according priority to getting young people and the long-term unemployed off benefit and into work, though also aimed at lone parents and disabled people who want to work.

Young people

The New Deal for 18-24 year olds will be introduced nationally in April 1998, after trails in 12 areas. Under this scheme, young people unemployed for over 6 months will be offered a choice between a job with an employer (who will receive a £60 (90 ECU) subsidy a week for 6 months, work in the voluntary sector, work for the new Environmental Task Force and an opportunity to study on a full-time approved course. Benefit sanctions will be applied to those young people who unreasonably refuse to take up a suitable option.

Long-term unemployed

The New Deal for the long-term unemployed will be introduced in June 1998, with subsidies to employers of £75 (110 ECU) a week for 6 months recruiting people of 25 or over who have been unemployed for two years or more and employment-related courses of education for the older unemployed for up to a year whilst continuing to receive benefit.

Gateway opportunities for the older long-term unemployed are also planned to be developed to provide more assessment, advice and help with basic skills.

Lone parents

The New Deal for lone parents involves the appointment of a personal caseworker to offer help and advice with job search, training needs, benefits and child-care. The scheme, which will be available to all those in receipt of Income Support from October 1998, is voluntary and is primarily aimed at lone parents whose youngest child is at school but is also available to lone parents with younger children. At the same time, the additional benefit payable to lone parents not in work will be withdrawn from October 1998, though this will be accompanied by a significant increase in child benefits for everyone, single or married.

The Netherlands: reforming the invalidity benefit system

The system of invalidity benefits in the Netherlands was created in 1967 and was characterised by wide coverage and generous levels of payment (70% of previous earnings — 80% before 1987 — up to the age of retirement). Between 1980 and 1990, the number of beneficiaries increased by 34% to reach 14% of the labour force, 80% of them being regarded as totally incapable of working, 40% because of psychological problems. In practice, the scheme conveniently reduced the number of people classified as unemployed, providing a higher level of income support for a longer period with no direct cost for employers.

In 1993, a number of reforms were introduced to tighten the criteria for eligibility, to require those drawing benefit to undergo periodic and more systematic medical examinations, to assess capacity for work in terms of the ability to do any job rather than what a person was doing before, to reduce benefit levels and to transfer the cost onto employers. The latter has been achieved by introducing a system under which contribution rates for employers are partly differentiated according to the number of their employees claiming disability benefits. Employers can opt out of the scheme by assuming the risk themselves (which they can insure against privately), but whether they do so or not, they have a clear incentive to reduce the number of workers registering as disabled, by both improving health and safety at work and keeping those with disabilities in employment, whereas previously there was no such incentive. By these means, it is aimed to reduce the number of beneficiaries significantly.

those of 30 and over) and people with no fixed abode, this has been accompanied by a stipulation that recipients have exhausted all other means of improving their situation and are actively seeking employment, unless they are 60 or over or disabled.

In Belgium, a recent measure is intended to make it easier for homeless people to work by giving those receiving *minimex* (minimum income support) a lump sum settlement allowance (of 27,000 BEF, around 650 ECU) to assist them find accommodation. At the same time, it has been made possible for employers providing communal, social or cultural services to take on *minimex* recipients and obtain relief from social contributions.

The potential role of communal services, and voluntary and non-profit-making organisations in particular, in providing employment for those either at present excluded from the labour market or difficult to place is being actively considered in a number of Member States, as a means of involving them more fully in economic and social life while producing services for which there is unmet demand (partly because of the constraints on public budgets). Such activities are most developed in the Nordic countries, though, as noted in Chapter 4, they have recently been expanded in Belgium. Moreover, in Ireland, a Green Paper on the role of the voluntary and community sector and its relationship with the statutory sector was published in 1997 as part of a National Anti-Poverty Strategy launched at the same time, which aims within a year to identify the structures required for the effective implementation of such a policy.

At the Luxembourg Jobs Summit at the end of 1997, national governments recognised the potential importance of the local economy as a source of new jobs, especially in social and environmental activities where apparent needs are not at present being satisfied by the market. They agreed in the Employment Guidelines to investigate measures to exploit these possibilities and to identify, and, where possible, remove, obstacles to their development.

People with disabilities

People with physical or mental impairments pose special problems for social protection policy in a similar way to lone parents. In a number of Member States, the Netherlands and the UK being among the most prominent examples, both the number receiving disability or invalidity benefits and the expenditure involved have risen markedly over the past 20 years or so, coinciding with the slowdown in economic growth and large-scale job losses in traditional industries. In many cases, shifting people out of work on to disability benefit schemes, especially older men who had been unemployed for a long time, was a way of reducing both the demand for the inadequate number of jobs available and the number registered as unemployed. The growth in the number involved and in the cost, however, led to increased concern in the early 1990s.

In recent years, in both the Netherlands and the UK, attempts have been made to tackle both aspects of the problem, in particular by introducing more stringent tests for assessing incapacity for work. In the UK, a new Incapacity Benefit came into effect in 1995 replacing Invalidity and Sickness Benefits, the principal change, in addition to a tougher medical test, being the introduction after 28 weeks on benefit of an assessment relating to a person's fitness to do any kind of work rather than the work they were doing in their previous job (as during the first 28 weeks). People failing the test have to register as unemployed and actively look for work. The result in the first year was a small fall in the number claiming benefit in contrast to the previous tendency for the number to increase.

In the Netherlands, responsibility for policing benefits has been partly shifted to employers, who have to pay higher contribution rates if more of their employees register as disabled, giving them a clear incentive to minimise the numbers opting to do so (see Box). This measure has been coupled with greater stress on helping people registered as having disabilities into work through active employment programmes. In Austria and Finland too, the emphasis of policy has shifted from income support to rehabilitation. In the latter, temporary invalidity benefits have been renamed rehabilitation benefits, the granting of which requires participation in a rehabilitation programme. In the former, entitlement to disability benefit has to be re-established every two years and is granted only if it has not proved possible to find employment for the claimant through rehabilitation measures.

Providing access to labour market programmes coupled with incentives for them to look for work is, however, not sufficient to bring about a substantial change in the position of disabled people in the economy or society. Such measures need to be accompanied by legislation to prevent discrimination against them in employment and in their access to goods, services and facilities of various kinds, so increasing their chances of finding a job and making it easier for them to use public transport and buildings, including offices and factories. In 1993, all Member States adopted the UN *Standard Rules of Equality of Opportunity for Disabled People* and in most of them, anti-discrimination legislation is in force (see *Employment in Europe, 1997*, Part II, Section 2, for a more detailed account of recent policy developments across the Union towards people with disabilities).

Curbing spending on sickness benefit

In a number of Member States, attempts have also been made to reduce expenditure on sickness benefits. In the Netherlands, as with disability benefits, responsibility for curbing spending has been shifted to employers, who from March 1996 have been obliged to continue paying salary to employees unable to work for up to 52 weeks, though they can take out private insurance against the eventuality. As a result, absenteeism seems to have fallen, but there are signs that employers have become more selective when they initially recruit people (despite legislation preventing discrimination on health grounds). It is also expected that there will be an increase in fixed-term contracts (temporary workers are still covered by the state scheme) and in the use of employment agencies.

In Portugal, increased efforts have been made to reduce fraudulent claims of sickness benefit and there is more frequent checking of incapacity for work. In consequence, expenditure has been reduced by a third. In Sweden, sickness and occupational injury benefits have been consolidated into a single scheme, the benefit rate being reduced in the case of the latter from 100% of former earnings to 80% at the same time, though the period over which they are paid was increased by 4 weeks.

Reversing the trend towards early retirement

Increasing employment, or more accurately postponing the effective age of retirement, has also become a more important aim with regard to older people. In most Member States, the higher levels of unemployment and inadequate rates of job creation from the mid-1970s on led to policies encouraging older people to withdraw from the labour force before the official age of retirement. Such policies took the form of early retirement schemes, with people able to receive pensions before the official retirement age, especially if they were unemployed, or special benefits for older workers as well as disability benefits, as discussed above. The escalating cost of early retirement, however, allied to the prospect in 10–15 years time of a substantial expansion in the number of pensioners as the post-war baby boom generation reaches retirement age, has caused a radical rethink of policy in recent years (see Chapter 5 for a more detailed account). The only area where such a rethink has not occurred is agriculture, where early retirement programmes have continued to operate with Union support in order to reduce the number employed in the sector.

Nevertheless, low rates of employment growth have ensured that, in most countries, there remains an awkward conflict between increasing the number of older people in work and reducing unemployment. Moreover, irrespective of the efforts or wishes of government, if people lose their jobs in the later years of their working lives, the lack of alternative employment may mean that they have little choice but to retire early. This might explain the continued increase in early retirement among men aged 55 and over in most parts of the Union, which by 1996 had resulted in around half of men aged 55 to 64 no longer being economically active and under 30% of women (see Chapter 5 for details).

The shift in attitude towards early retirement is evident in the tougher stance on disability benefits in a number of countries. In addition to the examples noted above, tighter restrictions on the receipt of early retirement pensions have been applied in Sweden, where claimants now need to demonstrate that they are incapable of working, so that, in effect, the payment has been transformed into a sickness or invalidity benefit. At the same time, the basic pension payable to those retiring early has been reduced by 6%, while there has also been a reduction in the pension payable to those married to someone below pensionable age, which is more likely to apply to those retiring early than at the normal age.

In both Germany and Austria, the conditions of eligibility for early retirement as well as invalidity benefit have also been tightened and the pension reduced. In Belgium, where retirement is possible for men between the ages of 60 and 65 (and will be for women once their statutory retirement age has been increased to 65), the number of years of contributions necessary to qualify for a pension is being raised and the contributions payable on early retirement pensions increased. In Spain, voluntary retirement before the age of 65 is now penalised by a reduced pension even if people have the number of years of contributions required for a full pension (except when the person concerned becomes unemployed), while in Greece, entitlement to early retirement pensions have been restricted and the overall amount paid reduced.

Moreover, in a number of countries, partial pension schemes, enabling people approaching retirement age to work part-time rather than full-time and receive a pension at the same time, have been introduced or extended with the primary aim of reducing the numbers retiring early (see Chapter 5 for details of these and the other measures noted above).

Adapting social protection to population ageing

As well as addressing the growing cost of early retirement *per se*, all governments across the Union have had to contemplate the implications for social transfers of the impending expansion in the number of people of pensionable age in 10–15 years time, in a context where the population of working age is likely to be either declining or remaining largely unchanged. The reform of pension systems aimed at managing the cost of this shift in age composition — or, more accurately, the scale of income redistribution which it entails — has, therefore, become a central item on the policy agenda in all countries. Irrespective of the systems in place, increasing efforts are being made to identify the changes required to contain the growth in expenditure implied by demographic trends and to put these into place early enough for them to be both effective and equitable. This longer-term concern has been overlain by shorter-term financing problems resulting from the slowdown in economic growth and fall in employment, which have depressed income from both taxes and contributions.

A common response to longer-term considerations (as described in more detail in *Social Protection in Europe, 1995*, Chapter 2 and in Chapter 5 below) has been to raise the official retirement age of women to bring it into line with that of men, for both cost and equity reasons. This is the case in Germany (where it will be progressively increased from 63 to 65 for men between January 2000 and December 2001 and from 60 for women to 65 between January 2000 and December 2004), Greece (from 60 to 65 for women insured since 1993), Portugal (from 62 to 65 for women by 1999), the UK (from 60 to 65 from 2010) and, more recently, in Belgium and Austria (from 60 to 65, from 1997 on in the former, though only from 2019 on in the latter, the process not being completed until 2033).

In all these countries, therefore, as in most other parts of the Union, the official retirement age has been, or will be, standardised at 65 for both men and women. This, however, has been coupled with increased emphasis on the contributions record of those retiring, or, in other words, on the number of years they have been employed, so linking the pension receivable more closely with the payments made over a person's working career and reinforcing the insurance aspect of the system. As a corollary, to avoid discrimination, specific concessions have been introduced for women to allow for the years they spend taking care of children or invalid parents, though the precise form these take and their scale vary between countries.

Nevertheless, in most Member States, the pension receivable on retirement bears little relationship to the amount actually contributed during a person's years in employment. In all Member States, with the partial exception for supplementary pensions of the UK, the Netherlands and Finland, pension systems are operated on a pay-as-you-go basis, so that the amounts paid out to those at present in retirement are financed from current contributions or revenue from taxes, paid largely by those in work or their employers. Increasingly, however, the rate of benefit is constrained by the finance received and is adjusted in various ways to be consistent with this, rather than rates of contribution or tax being modified to meet a larger pension bill.

In addition to raising the age of retirement, which will largely affect expenditure on pensions some time in the future, many governments have also reduced the effective rate in relation to past earnings by altering the pension formula. In particular, in France, Portugal, Austria and Finland — in the last, in the case of employment rather than basic pensions, which are flat-rate — the number of years of earnings on which the pension is based has been increased (from the best 10 to the best 25 in France, to the best 10 of the last 15 instead of the best 5 of the last 10 in Portugal, to the best 15 years instead of the last 10-15 in Austria and to the last 10 instead of the last 4 in Finland), so reducing the sum payable in most cases.

Moreover, adjusting the method of revaluing pensions for inflation has also proved a useful means of reducing the amount paid out. In France, indexation in recent years has been based on price rises rather than wage increases; in Finland, the index used was changed in 1996 to reflect prices much more than wages (weights of 80% and 20%, respectively, being used), while in Spain, the method of indexing has also been made less favourable. In Germany, indexing is now based on net rather than gross earnings, which when taxes and charges are rising also has the effect of reducing the amount paid (though equally it maintains the value of pensions constant in relation to disposable income in employment). In Sweden, more radically, pensions are not being fully indexed in line with wages so long as the budget deficit remains excessive.

In other countries, pensions have been reduced by other means. In Greece, legislation passed in the early 1990s not only discontinued the indexing of pensions to wages but raised the pensionable age of public employees, increased the minimum career length for retirement under the general scheme (KA/TEAM) and limited the pension payable to new entrants into the scheme to 60% of previous earnings. As a result, the number receiving the minimum pension has risen (to 71% of those paid from the National Insurance Fund — IKA — in 1996) and the value of this has fallen (from 20% of the average wage of unskilled workers in 1990 to 17% in 1995). In 1995, a million pensioners received benefit of less than half average income per head and 25% of these had no other means of support, prompting the introduction in 1996 of a means-tested allowance for pensioners over 60 (see Chapter 7 for ECHP data on pensions in Greece).

A similar measure has also been recently introduced in Spain, where the number of years needed to qualify for a full pension has been increased and the coefficient applied to earnings reduced. In both countries, therefore,

The direction of social protection reform in Spain and Italy

In Spain, following the recommendations of the 'Pact of Toledo', an 'Agreement for the consolidation and rationalisation of the social security system' between the Government and the two main trade unions was signed in October, 1996. This forms the basis of legislation introduced in 1997 to reinforce the contributory nature of the Spanish social security system, to split contributions equally between employers and employees and to increase expenditure on social protection to the average Union level. A permanent committee of government and the trade union representatives has been set up to monitor the implementation of these aims and to present proposals to the parliamentary commission responsible for social protection. The first major reform will establish a clear division, by the year 2000, in the financing of social protection, with insurance benefits financed by contributions and universal non-contributory transfers and direct spending on goods and services financed from general taxation.

In Italy, at the beginning of 1997, the Government appointed the Onofri Commission, a group of experts, to outline broad guidelines for a modernising the social protection system. Its main recommendation was to correct the bias of the system towards retirement pensions and certain privileged groups (such as employees of large private enterprises and civil servants) and to increase spending on social assistance, social services and active labour market measures. The specific proposals included:

- implementing fully the 1995 pension reform, in particular harmonising the different occupational schemes;
- distinguishing social insurance benefits from social assistance and financing the former from contributions, the latter from general taxation;
- introducing more rapidly a 'defined contributions' system for pensions and strengthening its contributory principles;
- raising the lower age limit of 57 for flexible retirement;
- increasing the incentives for the development of occupational pensions;
- establishing a minimum income scheme based on need;
- establishing a new fund for those in need of long-term care;
- replacing the highly fragmented system of unemployment compensation by two unitary schemes, one for temporary lay-offs (70% of previous earnings initially, with a declining rate, for a maximum of 12–18 months in five years), the other for unemployment proper (60% initially, with a declining rate, for up to 3 years).

In June 1997, official negotiations started on the reforms, the two most controversial issues concerning the proposed rationalisation of pension arrangements, which means reductions for some groups, and of unemployment benefits.

In November 1997, agreement was reached between the Government and trade unions on a small reduction in the transition period and an acceleration of the convergence towards uniform rules for the various schemes (which was included in the 1998 budget law). The same agreement reaffirmed the need to encourage, possibly through financial incentives, some form of flexible and gradual retirement.

a reduction in the level of pension has led to increased reliance on means-testing. This has also been the case in Sweden as a result of reductions in housing supplements paid to pensioners, coupled with the partial indexing of pensions, as noted above.

In Sweden as well, the pension payable to those married to someone below pensionable age has been reduced, while widows' (or survivors') pensions were made subject to an income test in 1997, so reducing the amount received by those with income above a certain level. Moreover both in Sweden and Finland, measures have been introduced to withdraw the basic, flat-rate, state pension from those whose earnings-related 'employment' pension is considered sufficient, so effectively transforming the basic pension into a supplement, while in Finland, increased amounts for dependent spouses and children will no longer be included in the basic pension.

Proposals for future action

Throughout the Union, there is ongoing debate about the need for pension reform in the light of the future growth in the number of people in retirement and, in particular, about the respective roles of basic, supplementary, occupational and private schemes. So far, however, there has been no significant tendency to shift away from pay-as-you-go to funded schemes (ie where income is accumulated from contributions to cover future pension liabilities). Nevertheless, in a number of Member States, measures to increase the importance of occupational and private schemes to supplement basic pensions and to relieve the State of part of the liability for financing future payments have either been introduced or have been proposed. There are also signs of a shift towards defined contribution systems, where the pension received on retirement is determined by contributions paid over a person's working career instead of earnings over a given period, so reducing some of the difference between pay-as-you-go and funded systems.

Debate is particularly lively in Southern Member States because of concern about features of existing systems. In Spain, following the Pact of Toledo between Government and the social partners (see Box), there are plans to encourage voluntary private schemes to supplement state pensions and to give fiscal incentives for these to be organised on a collective rather than individual basis (so that premiums are the same for everyone irrespective of their personal circumstances). At the same time, a reserve fund has been established from the annual surpluses generated by pension funds to help cover the future costs of demographic trends. In Greece, where the system is particularly fragmented, there is ongoing debate aimed at rationalising the social security system as a whole.

In Portugal, the possibility of limiting the future amount of pension by imposing a ceiling on earnings to which pensions (and contributions) relate is being debated, as is the incentive which this would give for the development of supplementary schemes, whether private or public. At the same time, there is concern about the need to find finance from elsewhere in the event of a ceiling being imposed, about the increase in saving which the growth of supplementary schemes would imply and about the importance of regulating occupational schemes to protect workers. In addition, in Ireland, a *National Pension Policy Initiative* was launched in 1996 for debate on future policy, and proposals are due to be published by mid-1998.

In Italy, the Onofri Report called for the more rapid implementation of the proposals put forward in 1995 for a unified system (see *Social Protection in Europe, 1995*, Chapter 2 for details), under which pensions will be based on contributions rather than earnings and the development of voluntary supplementary pensions will be encouraged (see Box). In Sweden, a similar shift towards a defined contributions, rather than defined benefits, system was proposed in the reform measures announced in 1994. Though, like the Italian system, this will remain largely pay-as-you-go, and will be compulsory, 2% of earnings will be put into a fully-funded scheme where individuals decide the placement and management (ie a state system with an element of individual choice, representing a compromise between opposing political viewpoints).

In Germany, the Federal Government in 1997 put forward proposals for further reform of pensions to reduce the standard amount payable, from 70% of previous net earnings to 64% by 2030, with the aim of avoiding increases in contributions. In addition, funding for pensions from the Federal Budget has been increased by raising VAT from 15% to 16% from April 1998. Although there have been some proposals to limit state pensions to a basic amount, the consensus among the two main political parties is to retain the main features of the present system, namely, contributions and benefits related to earnings and pay-as-you-go financing.

The same consensus is also evident in Austria, although here the insurance principle has been strengthened under the *Pension concept 2000* reform by including stronger actuarial factors in the calculation formula for early retirement pensions which could encourage people to stay longer in employment and so raise the actual age of retirement, the aim being to safeguard the financing of Austrian pensions over the medium and long-term.

In France, legislation was introduced by the previous Government in 1997 enabling tax incentives to be given to encourage the development of supplementary funded schemes for private sector employees. The new government, however, has delayed its implementation, fearing that it would jeopardise the current pay-as-you-go supplementary schemes (ARRCO and AGIRC) managed by the social partners.

The main countries in the Union where the pension system has developed in a radically different way are the UK and Ireland. In the former, an estimated two-thirds of pensioners have an occupational or private pension and the state benefit is relatively low. Accordingly, substantial numbers, mainly the one-third without a private pension, rely on means-tested income support to sup-

Safeguarding supplementary pensions

As governments across the Union seek to limit the growth of state pensions, supplementary schemes, in the form of occupational or private pensions, are becoming increasingly important as a means of enabling people to maintain their income at a satisfactory level when they retire. The development of such schemes, which are generally on a fully-funded rather than a pay-as-you-go basis and which serve to take some of the pressure off the State for meeting the aspirations of people for a decent income in retirement, requires, however, a secure environment, which only governments can create. In particular, a regulatory framework is needed which safeguards the assets accumulated in a pension fund, notably in the event of an employer's insolvency or the transfer of ownership of a company. These principles have been agreed at Community level and are laid down in Directives 80/987/EEC and 77/187/EEC.

They need, moreover, to be accompanied by the provision of clear, understandable and unbiased information to workers so that they are able to choose between alternative schemes, in full awareness of the management costs involved and the pension they are likely to receive on retirement under different assumptions about future developments.

The regulatory framework must also establish the principle of equal treatment for men and women, as set out in the 1996 'Post-Barber' Directive (of December, 1996, Directive 86/378/EEC concerning equality between men and women in occupational social security schemes).

The growth of supplementary schemes implies a concomitant growth of pension funds which has implications for the development of the European capital market in the context of economic and monetary union, as well as for the free movement of labour. These implications and the potential for investment in industry and infrastructure are examined in the Commission Green Paper, *Supplementary Pensions in the Single Market* (COM (97) 283, June 1997.

plement the basic amount, though it is estimated that up to 1 million fail to claim (and receive) the supplement they are entitled to. In Ireland, over 50% of employees at work have occupational or personal schemes and the State provides only basic flat-rate cover. A major proportion of future pension liabilities in both countries is, therefore, fully funded and managed by private insurance companies, leaving the state to take care of the less well-off and those who have failed to build up an adequate pension for their retirement.

The main focus of policy in the recent past has been on strengthening the regulations governing private pension funds to prevent a repetition of the problems experienced in the last few years — specifically, the fraudulent use of pension fund money by employers responsible for managing it and the misleading selling of private schemes. ($1\frac{1}{2}$ million people are estimated to have been wrongly advised to switch from occupational to private schemes and, under pressure from the Government, restitution by the insurance companies is now gradually taking place.) This concern echoes that expressed in Community Directives aimed at ensuring the establishment of a sound regulatory framework for supplementary pensions as they increase in importance across the Union (see Box).

Soon after coming to power in 1997, the new British Government announced a pension review to examine central areas of insecurity for elderly people, including the relationship between basic and second pensions, the appropriate balance between public and private and the proper regulation of the latter, the importance of raising awareness of the need for a pension and a narrowing of the pensions gap between men and women. It also announced a pension-sharing plan for divorcing couples from the year 2000 and the development of 'citizens' pensions' for carers unable to contribute to a pension scheme and 'stakeholder pensions' for those on low incomes or with changing patterns of employment.

It appears, however, that no major shift away from the previous Government's policy orientation, with its emphasis on private sector involvement, individual responsibility and the accumulation of savings in pension funds to cover future liabilities, is planned. Whether this approach is better designed to overcome the transfer problem inherent in the future growth in the proportion of people above pensionable age than that being followed in the rest of the Union is by no means clear. Ultimately, the effective transfer of income from those in work to those in retirement has to be made, irrespective of the way in which it is achieved, and the ease of doing this — in terms of the avoidance of social unrest and the maintenance of social cohesion — will depend largely on the income available to be distributed. It is a matter of debate which of the two approaches is more likely to deliver the economic growth required to secure this or which is putting the greater financing burden on future generations. Ultimately also, unless there is a fundamental change in philosophy, the State is responsible for ensuring an adequate level of pension for everyone, irrespective of the role played by private insurers and the attempts made to persuade individuals to assume responsibility for their own actions.

Restraining the costs of health care

The constraints on public expenditure have focused particular attention on health care services, the demand for which tends to rise rapidly as real income increases and medical know-how expands. The growth in demand has been boosted further by the increasing number of people living into old age. The widespread response in Member States has been either to limit expenditure directly, where services are managed by the State or to impose ceilings on spending growth, where this is determined by health insurance funds. The key issues in this context then become how expenditure is allocated between both the services provided and the people receiving care and how efficiency in the use of available resources is assured. The response in many countries has been to introduce market, or pseudo-market, mechanisms, as discussed in some detail in Chapter 6 below.

In a number of Member States, global budgeting has been introduced to curb the growth of health insurance fund expenditure. In Germany, this has been the case since 1993 and in France, for public sector hospitals since the 1980s and private ones since the beginning of the 1990s, though general practitioners remain outside the system of controls (the proposal in the *Plan Juppé* to include them met severe opposition). In Belgium, growth rate norms of $1\frac{1}{2}\%$ a year were imposed a few years ago and have been extended to the year 2000, while fees charged for treatment have been frozen or even reduced. In other Member States, where national health services exist which tend to be organised on a regional basis, a common focus has been on limiting the budgets of regional authorities and making them more accountable for any 'excess' expenditure incurred.

At the same time, in many Member States, charges for drugs and certain kinds of treatment — 'co-payment' — have been increased and/or extended. This has been the case, for example, in France, where charges for hospital stays went up in 1996, in Germany, where the co-payment required of patients has been raised repeatedly, and in the Netherlands, where since January 1997, most people pay 20% of the cost of treatment, with certain exceptions, up to a maximum annual amount. The objective of such measures is both to reduce the cost falling on the state and to make consumers more aware of the cost of their actions, so encouraging them to be more rational in their demand behaviour.

Indeed, the general motivation for introducing market mechanisms into health care systems, as has occurred most notably in the UK and the Netherlands, is to increase efficiency by forcing people to take account of the cost implications of their decisions. This involves, of necessity, making a clear distinction between purchasers and providers — between health authorities and general practitioners, on the one hand, acting on behalf of the patient, and hospitals and specialists, on the other — which often tends to be blurred, so enabling purchasers to exercise financial discipline over providers, encouraging contracts detailing terms, conditions and the specific services required to be drawn up and opening the way for competition on both sides.

Such action also provides greater scope for the exercise of managerial expertise, an objective, for example, of the Italian reforms of the early 1990s as well as of the draft bill recently presented in Greece. So far, however, difficult choices of how to determine the allocation of resources between different areas and of how far to limit the care and treatment freely available within the public sector — or at least at nominal charge — remain largely unresolved. Moreover, there is as yet no general solution to the problem of reducing the high level of dissatisfaction with public health services, which is evident in many Member States at present, without adding significantly to expenditure.

Care of the elderly

The impending growth in the proportion of the population of pensionable age is also serving to focus attention on the implications for health care and support services. The demands imposed on both of these increase considerably as people age, as noted in Chapter 1. A significant proportion of the very elderly tend to be frail or infirm and accordingly in need of everyday care, and there is little sign that this proportion is declining over time. This care has traditionally been provided from within the family. But the gradual disappearance of the extended family, the increased likelihood of different generations living some distance apart and the much greater numbers of women in paid employment have made this less feasible. At the same time, there is a common shift in policy across the Union away from the provision of residential care towards providing the support and services — home-help as well as medical care — required for people to continue living at home.

The debate at present in a number of Member States, partly prompted by the introduction in Austria in 1993 and in Germany in 1995 of a scheme for long-term care, is over the extent to which the provision of such care should be part of the social protection system rather than being left to individuals to organise themselves. This comes down essentially to a choice between increases in social charges and/or taxes to fund the social transfers and/or direct expenditure on services required and accepting the consequences of relying on personal responsibility. The latter consist not only of the distributional effects of an unequal cost falling on different individuals, and, specifically the poorer rather than the richer sections of the community, whether they take out private insurance cover or not, but also of the response of the State to the possibility of increasing numbers of people being driven into poverty by having to meet the costs of care.

A further issue concerns whether protection should take the form of direct services — the option chosen in the Nordic countries, in particular — or transfers, as in Germany and Austria, giving the beneficiary a choice over how to spend these. Though the latter opens up the possibility of competition in service provision, it also encourages the development of informal as opposed to formal arrangements and, therefore, is likely to give rise to fewer jobs. In either case, additional issues arise as to how services or transfers are allocated and, accordingly, how the need for care is evaluated, and how far social services or transfers should be targeted on those with income below a certain level.

In Member States, there have been concrete developments in this area as well as discussion of options (see Chapter 7 for more details). In Germany, benefits for care at home under the new social insurance scheme (*Pflegeversicherung*), began to be paid in April 1995, and in July 1996 benefits for residential care were introduced, both financed by social contributions levied on employers and employees (though with a loss of one day's holiday to compensate for the effect on labour costs). In Austria, a new attendance allowance, *Bundespflegegeld*, was introduced in 1993, payable to all those with disabilities and/or chronic illnesses in need of at least 50 hours of attendance or care a month and administered by the social insurance institutions, the Federal Government and the 9 Länder, though funded from general taxation.

Elsewhere, a draft bill was published in Luxembourg in 1996 for the introduction of a compulsory 'dependence insurance' scheme to cover care and assistance required by those unable to take care of themselves. In Italy, the Onofri Report called for a new fund to be established for long-term care, while in Ireland, the means-tested Carer's allowance (for those looking after elderly relatives) was extended and the conditions for eligibility eased.

In the Nordic countries, increasing constraints on expenditure on social services and support facilities have been imposed, leading to a growing concern over the under-provision of services, though there has been little questioning of the role of the State in this area. In the UK, with the implementation of the *Care in the community* programme, responsibility for providing long-term care has effectively shifted from the National Health Service to local authorities, whose budgets have also been tightened, as well as to families and voluntary organisations, which have to contend with the consequences of under-provision.

Shifts in sources of finance

The concern on the expenditure side to reduce the number of people dependent on social transfers and to encourage them to become employed has been accompanied on the financing side by a widespread policy of reducing social contributions levied on employers and broadening sources of revenue. The motivation is both to spread the cost of social protection more evenly across society — and the economy (ie away from employment) — and to encourage job creation.

While in all Member States, social protection systems are funded partly by contributions and partly from taxation, the relative weight of the two differs substantially (see Chapter 3). Irrespective of the weight, however, there has been a general attempt to stabilise or reduce rates on employers in order to contain labour costs, though this has not always been successful in a context of slowly growing real income and rising unemployment (in Germany, for example, the rate of pension contributions on earnings rose from 17.5% in 1993 to 20.3% in 1997 primarily because of this rather than a growth in expenditure on pensions).

The aim of cutting charges levied on employers has been coupled with a concern to retain and even strengthen the contributory aspect of the system, in part to emphasise the insurance dimension and the link between paid employment and access to benefits, in part to limit eligibility for benefits and so reduce expenditure. Indeed, in Denmark, where social expenditure has historically been funded almost entirely from taxes, contributions have been recently introduced with precisely these aims. By 1997, employees' contributions had been increased to 8% of gross earnings with a compensating reduction in income tax. In Spain, a major objective of the 'Pact of Toledo', ratified by Parliament in 1995, was to reinforce the contributory nature of the social protection system and to reaffirm the principle of an equal division of charges between employers and employees, while in Austria, compulsory social insurance contributions were recently extended to new forms of atypical employment.

In the latter two countries, however, as well as elsewhere, there have been increasing attempts to distinguish between benefits paid to those previously in employment, which are generally related to earnings (eg unemployment benefits), and benefits payable to all (eg health care or family benefits), the idea being to reduce the use of contributions as a source of finance for the latter and, so far as possible, to confine them to funding the former. Such attempts have been accompanied in some countries by greater (if limited) use of 'earmarked' taxes in order to emphasise the link between taxation and benefits and, accordingly, to reduce resistance to the introduction of new taxes and engender solidarity.

In Belgium, the attempt to reduce reliance on contributions has been accompanied by an increase in VAT, especially on fuel — as it has in Luxembourg — though the amount of revenue raised from new alternative sources is still relatively small (only 5% or so in 1996). At the same time, there has been an extension of social contributions to cover students for the first time (with a charge of 5% on earnings for employers and 2.5% for employees) and the use of company cars (33% of the value of the benefit in kind). In addition, employers' contributions have been increased by 10% to fund special unemployment schemes.

In France, the CSG (*Contribution Sociale Généralisée*), the 'solidarity tax' introduced in 1989 to replace part of contributions for old-age and family benefits, was raised to 3.4% in 1995. A proposal made at the same time to extend the charge to health care in place of health insurance contributions levied on earnings has been taken up by the new Government. A new charge to help pay off accumulated debt on social expenditure — *Contribution pour le Remboursement de la Dette Sociale* — was also announced in 1995 at a rate of 0.5% on earnings and social insurance benefits.

In Portugal, employers' contributions were recently reduced by 0.75% of earnings. At the same time, a new 'social' VAT of 1% was created to make good the loss of revenue. In addition, there is active consideration of the possibility of reducing employers' contribution on part-time work as well as of cutting them further relative to the rate levied on employees generally, a course of action which has already been followed in a number of countries, particularly Sweden.

In Germany, despite the growing emphasis on the need to keep down contributions on employers, the new long-term care benefit was funded by an increase in contributions (divided equally between employers and employees), though the effect on labour costs was offset by reducing paid holidays by one day a year, the rate being raised further in 1996 when benefits were extended to cover residential care. However, the Employment Promotion Act has been repeatedly amended with a view to stabilising contribution rates, which has led to a number of cuts in benefit levels and a tightening of eligibility criteria in recent years.

At the same time, selective reductions in employers' contributions have been used as a means of encouraging the employment of those who have difficulty in finding jobs, especially young people and the long-term unemployed. These, however, are equivalent to direct subsidies and should be regarded as part of active labour market measures rather than as part of the general attempt to alter sources of finance, especially since they have been associated in some Member States with upward pressure on the general rate of social contribution rather than with an increase in other forms of funding.

In Belgium, for example, reductions in contributions have been combined with direct subsidy as a means of stimulating job creation. Employers creating socially-useful jobs, for instance, receive both a large subsidy for three years and full relief from social contributions. In the UK, employers taking on people unemployed for two years or more are also exempt from social contributions, in this case, for a year, while in France, the previous Government subsidised recruitment of the long-term unemployed, both directly and through reductions in contributions, and also lowered contributions for employers taking on lower-paid workers (those with earnings at the same level as the SMIC and up to 20% more than this).

Indeed, in France, the cost of various measures to subsidise employment was estimated at 4% of GDP in 1995, which, because of the seemingly small impact on unemployment, has led the present Government to divert the resources involved into plans for creating 700 thousand jobs for young people at the SMIC rate of pay. At the same time, it has announced plans to repeal the cut in social charges to employers reducing working time and taking on new workers (40% initially for those reducing average hours worked by 10% and 50% for those reducing them by 15%) and to replace the scheme with a general cut in working hours from 39 to 35 hours a week.

Concluding remarks: the scope of social protection and targeting

As indicated in the above analysis, the focus of most of the recent changes in systems of social protection across the Union has been on the twin aims of containing costs and reducing dependency by getting people into work. The latter objective has been emphasised in recent Commission declarations, particularly in the Communication on *Modernising and Improving Social Protection in the European Union* and was recently taken up at the Luxembourg Job Summit, where Member States reaffirmed the importance of moving from passive measures of income support to active policies for improving employability.

In Southern Member States, this has gone along with efforts to rectify gaps in the protection provided, to balance the provision of support more equitably and to move closer to Northern European social welfare standards. At the same time, in Northern Member States, the universal systems established have come under increasing scrutiny, prompted by cost and dependency considerations. Debate has centred on both the scope of social protection, and the role of government within this, and, with tightening budget constraints, on the way that available finance is allocated between functions and people.

So far, in general, the consensus on the desirability of maintaining the universal nature of social protection accessible to all has held firm. Nevertheless, there is evidence of a shift in responsibility from the state to the individual in certain areas, which in some degree goes along with the aim of reducing dependency, and accompanying this, a shift from state to private sector provision. Examples are the effective privatisation of sickness and invalidity benefits in the Netherlands and the growth of private pensions in the UK. In both cases, a primary aim was to reduce public expenditure, or the liability of the state for future spending, though in each case government has maintained responsibility for managing the system and for acting as provider of last resort for those not adequately protected. Another example is the contracting out of certain social services, such as cleaning for the elderly and nurseries, in Denmark, a country where the notion of public provision of welfare services is deeply entrenched.

Privatisation, however, in the sense of the private, profit-making, sector being involved in providing social protection has not developed very far in most countries, and there is little sign, outside of the provision of supplementary pensions, that any significant growth is likely in the foreseeable future. Much the same can be said of targeting, at least in the sense of means-testing. Outside of Ireland, the UK and Spain, means-tested social transfers account for only a very small part of the total paid and in most countries have not increased significantly in relative terms (see Chapter 3, though the data available extend only to 1995).

There are, however, exceptions, such as the greater reliance on means-testing for pensions in Greece with the reduction in the real value of old-age pensions, the linking of family benefits to income in Greece and Portugal, or the introduction of a guaranteed minimum level of income for all in the latter, though this represents an addition to expenditure rather than a shift in the type of support given. In addition, in some countries, Germany in particular, the prevalence of means-testing has increased in the recent past as a result of economic developments, in the form especially of a growth in long-term unemployment, rather than because of any change in philosophy concerning the provision of support.

This lack of change may reflect in part a recognition of the problems associated with means-testing, which relate to the difficulties of ensuring that all those who need support actually receive it and the disincentive effects on work effort and job search associated with the withdrawal of benefits as income increases. Although such effects can be moderated, in the first case, by providing sufficient information about the scheme and helping people to claim the benefits for which they qualify and, in the second, by reducing support gradually rather than abruptly, such measures can add substantially to costs.

Targeting, however, does not necessarily imply means-testing. In Ireland, for example, the concern to reduce poverty has focused on children since these are regarded as a prime source of the problem. More generally, targeting has been associated with reducing social transfers made to those on higher incomes rather than restricting them to those on low incomes. This has been achieved both through setting a ceiling on the amount of support receivable and through taxing benefits and/or making them subject to social contributions. The latter serves not only to redistribute the net gain from transfers from those towards the top of the income scale to those further down but also to spread the cost of financing more widely, an increasingly justifiable aim given the growth in wealth of many pensioners.

Moreover, taxing benefits, or rather including them in the income on which tax liability is assessed, does not necessarily give rise to the same disincentive effects as means-testing. So long as it is associated with the integration of tax and benefit systems, it opens the way for the design of a coherent schedule of deduction rates which ensures that the system as a whole operates as intended as regards incentives to look for work or to seek to better personal circumstances. The desire to move towards such an integrated system is a common feature of the debate on the reform of social protection systems which is now being conducted across the Union. At the same time, however, the administrative costs of including everyone within the ambit of the tax system represents a significant obstacle.

Chapter 3 The scale of social protection and its effect on income

This chapter is concerned with quantifying the scale of expenditure on social protection in the Union, its growth over time and its effect on household income. It is divided into two parts. The first part examines trends in social spending and the way in which it is financed and is based on data from the revised ESSPROS (European System of Social Protection Statistics), covering, in particular, the period from 1990 to 1995. The second part analyses social transfers in relation to household income and focuses, in particular, on their effectiveness in providing income support to households with little or no earnings from employment and other sources. This is based on data which have only recently become available from the new European Community Household Panel. Whereas the first part, therefore, is based on expenditure data from administrative sources in the Member States, the second part uses information from the recipients of social benefits themselves, which is the only real basis for assessing the extent of protection provided by the systems in different countries.

Part 1 Trends in social expenditure and its financing

Expenditure on social protection is a major part of public spending in all Member States of the Union. In 1995, according to the new ESSPROS system of accounts, it amounted to around 28½% of GDP in the Union as a whole, equivalent to an average of some 4,800 ECU for every person living there. Around 70% of this expenditure, however, consists of transfers rather than direct spending on goods and services (the latter mainly comprising expenditure on health care) and is, therefore, not a component of GDP as such but an element in the way that the income generated by economic output is used. In other words, just under 20% of income in the Union is redistributed in order to provide support to those who are retired, unemployed, in ill-health or disabled, have children or have inadequate means of support from other sources.

How far such income is redistributed from the wealthier members of society to the poorer members as opposed to being transferred between those with similar levels of income, or even from the less to the more wealthy, is an issue examined in the second part of this chapter. In the first part, the scale of expenditure on social protection in different parts of the Union is examined as well as its composition, the way that it has changed over time and the relative importance of the different means of financing it.

One major qualification of the analysis needs to be made at the outset. Specifically, the data which are analysed in the first part relate largely to expenditure on social protection, measured as gross transfers from government to individuals. They, therefore, leave out of account two elements which are potentially important and which are liable to distort comparisons between Member States of the cost imposed by systems of social protection. The first are the taxes and social charges imposed on transfers in a number of countries, which reduce both the net income of recipients and the net cost to government insofar as the revenue which they yield is available to help finance expenditure. The second is the protection provided through tax concessions and allowances rather than direct transfers which reduces government revenue rather than increasing spending, though which in terms of the support provided and the effect on the need for finance may be identical. The first element means that the gross expenditure figures reported here overstate the cost of social protection and the extent of redistribution in a number of countries, as well as at the Union level The second means that both tend to be understated.

The scale of social expenditure

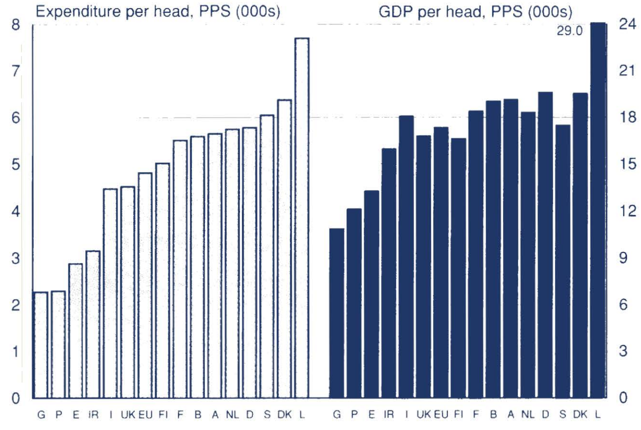
The average level of spending on social protection across the Union conceals marked differences between Member States. In terms of a comparable unit of measurement — purchasing power standards (PPS), which take account of differences in price levels as well as in exchange rates between countries — expenditure in 1995 ranged from under 2,500 PPS in Greece and Portugal and just under 3,000 PPS in Spain and just over in Ireland to over 6,000 PPS in Denmark and Sweden and over 7,500 PPS in Luxembourg (Graph 18). In between these extremes, spending in Italy and the UK was just below average and in Finland just above, while in the other 5 Member States, it was relatively similar at between 5,500 and 5,800 PPS. (Social protection is here defined as in the ESSPROS core system and covers the range of social benefits conventionally included in the term — see Notes and sources at the back of this Report.)

In relation to GDP, the variation between Member States was slightly narrower, ranging from 20% in Ireland and 21–22% in Greece, Portugal and Spain to just over 34% in Denmark and around $35^{1}/_{2}$% in Sweden (Graph 19). This pattern of variation is broadly in line with relative levels of prosperity, as measured by GDP per head, which is generally higher in the countries where expenditure on social protection is comparatively high relative to GDP (such as Denmark or the Netherlands) and lower in the countries where it is less (such as Greece and Portugal). In other words, there is some tendency for countries to spend more on social protection — or, more accurately, to redistribute a higher proportion of income in the form of social transfers — as they become wealthier and more able to finance it.

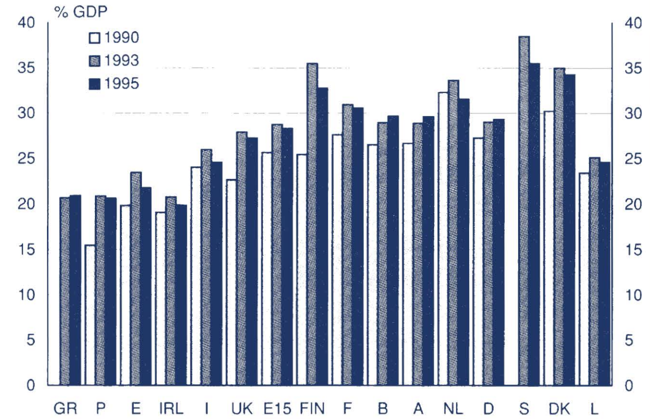
This tendency, however, is by no means systematic and it is clear that there are other factors influencing expenditure on social protection across the Union in addition to the level of income, quite apart from differences in the demands imposed on social welfare systems arising from variations in the age composition of the population and levels of unemployment, for example, as indicated in Chapter 1. In particular, it is evident that social expenditure is higher in the three Nordic countries, especially in Finland and Sweden, than in other Member States with similar levels of prosperity (such as the UK in the case of Finland and Sweden) and lower in Italy (which has a level of GDP per head only slightly lower than the Netherlands or France) and Ireland.

In the Nordic countries, a large part of the difference lies in greater expenditure on benefits in kind rather than cash transfers (which amounted

18 Social protection expenditure and GDP per head in Member States, 1995



19 Social protection expenditure in relation to GDP in Member States, 1990, 1993 and 1995



GR, S no data for 1990; DK 1993=1994; E15 for 1990 estimated for missing values to almost 14% of GDP in Sweden, just over 11% in Denmark almost 10% in Finland, well above the Union average — 8% — in each case), which, in turn, reflects the more extensive nature of social services in these three countries than in the rest of the Union. In Italy, on the other hand, less expenditure than elsewhere goes on benefits in kind (only $5^1/_2$% of GDP), partly reflecting the fact that the activities performed by social services in the Nordic countries tend to be carried out within the family, which is also the case in Ireland as well as in other Southern Member States. These differences, in turn, reflect the differences (as noted in Chapter 1) in both the structure of households — in particular, the much larger proportion of people living alone in the Nordic countries than in Italy or Ireland — and in the relative numbers of women in employment, which are still comparatively low in the latter two countries.

The differences in levels of social expenditure, however, also arise from differential rates of taxation and social charges levied on transfers, which, as noted at the outset, mean that the figures for gross expenditure described above are liable to give a misleading impression of the relative cost of social protection across the Union. Tax and social charges on transfers tend, in practice, to be relatively high in the countries where expenditure is highest, specifically in the three Nordic countries and the Netherlands, where they are used as a means of reducing the benefit from transfers going to wealthier households and, therefore, of targeting support on those most in need, and relatively low or zero in countries where it is lowest. Accordingly, it is safe to conclude that differences between Member States in the level of spending measured net of such charges are less than in gross expenditure.

Estimating the scale of the revenue involved and the extent to which net government spending is correspondingly reduced in the Member States in which charges are levied on social transfers is, however, fraught with difficulty and inevitably subject to some uncertainty. Estimates produced in a recent OECD study ('Net public social expenditure', *OECD, Labour Market and Social Policy Occasional Papers, No.19*) put the revenue yielded by direct taxes and social contributions on benefits at almost 6% of GDP in the Netherlands, over 5% in Sweden, 4% in Denmark and $2^1/_2$% in Germany, whereas in the UK, the figure was virtually zero. Taking account also of the revenue from indirect taxes as beneficiaries spend their transfers — which is more similar between countries — would reduce expenditure on social protection in net terms to around 27% of GDP in Sweden in 1995 and to between 23% and $25^1/_2$% of GDP in the other four countries (if the OECD estimates of revenue yielded by social transfers are applied to the ESSPROS data on gross expenditure). The difference between these countries is, therefore, narrowed significantly.

Moreover, measuring spending in net terms also affects the ranking of countries as regards expenditure on social protection. For example, the cost of the system in the UK in these terms seems to have been slightly higher in 1995 relative to GDP than in Germany or the Netherlands, whereas in gross terms it was lower.

Unfortunately, the OECD estimates relate only to the five Member States listed above and then solely for a single year. The latter is particularly unfortunate since it would seem from policy developments across the Union that charges imposed on social benefit recipients have tended to increase in recent years, in part to curb costs, in part to distribute the cost of financing systems more evenly across society. This means that the changes in expenditure examined below are likely in certain countries to overstate the changes in net terms which have occurred and, accordingly, to exaggerate the financing implications. Until further research is carried out to produce a complete set of estimates for net expenditure in all Union countries, for at least the most recent years, the extent of exaggeration, however, will remain unknown. (In this regard, it should be noted that it is the intention of Eurostat to develop a special module to take explicit account of the effects of taxes and other charges as part of the ESSPROS system.)

A further insight into the relative importance of social transfers in different Member States can be gained from the European Community Household Panel (ECHP) data which are analysed in Part 2 of the chapter and which show some differences from the figures on expenditure.

The other potential source of distortion is the exclusion from the analysis of tax concessions, allowances and rebates which serve a similar function to transfers in redistributing income towards particular groups considered to merit support, such as families with children or people taking out private pensions or private medical insurance. (Relief from social contributions is also excluded, though this is generally used to encourage employers to take on people who have difficulty in finding work and so is part of active labour market measures rather than social protection as defined here.) Like the revenue collected from social benefits, the value of these so-called tax expenditures is difficult to assess — as well as sometimes being hard to define — and, though estimates are made in a number of countries of the budgetary implications of particular measures when they are introduced, no complete and coherent set of estimates is available for Member States. At the same time, the indications are that the amounts involved in most countries tend to be relatively small — though there are exceptions, such as in the UK where tax relief on private pension contributions is important and ought to be included in the overall cost of pension provision — and do not appear to be systematically related to the level of direct expenditure on social protection. Accordingly, their inclusion might not change the conclusions reached from the expenditure figures too much (though inevitably there is some uncertainty about this).

The pattern of social expenditure

There is some variation in the composition of expenditure on social protection across the Union, which partly reflects differing needs, such as differential rates of unemployment or variations in the age structure of the population, partly differing priorities and partly differences in the organisation of the system or differing ways of providing support (such as to those out of work). There are, however, broad similarities between most countries as well as distinct differences. (It should be emphasised that, though the data broadly conform to the ESSPROS system of classification, there are divergences from this in a number of cases; these are listed in Notes and sources at the back of this Report and should be borne in mind when interpreting the figures presented here. Moreover, no data on the structure of expenditire are as yet available for Greece.)

In all Member States, except Ireland, old-age pensions (including survivors' benefits) are by some way the largest item of social protection expenditure, accounting for 42½% of the total in the Union as a whole in 1995, equivalent to 12% of GDP (Table 1). In most countries, the share of pensions was in the range of 35 to 45%, with only two countries, Finland (32%) as well as Ireland (25%) having a share below this and only one country, Italy, having a share much above. Indeed, in Italy, pensions represented almost 63% of total social spending, or 15% of GDP, substantially higher than in any other country, though part of this is due to the allocation of some transfers to this category which in other Member States are included elsewhere (early retirement pensions, for example — see Notes and sources). The high figure, however, also reflects the large proportion of the population above the official retirement age (62 for men, 57 for women) as well as the relatively large numbers below this age who are retired (40% of men in the 55 to 59 age group were not part of the labour force in 1996 and 20% of those aged 50 to 54; see Chapter 6 below). By contrast, in Ireland, the proportion of older people was much less than anywhere else in the Union (11½% were 65 or over in 1995 as opposed to 16½% in Italy).

The second largest item of expenditure in the Union is health care, accounting for 22% of the total in 1995 (some 6% of GDP), so that with old-age pensions, it represents almost two-thirds of the social protection budget. Since a large part of health care goes to older people, support for the elderly in various forms underlies much of the effort devoted to social protection in the Union. Only in the three Nordic countries did health care account for a significantly lower share of spending than 20%, though of these only in Denmark (where it was lowest of all at only 14% of the total) was expenditure markedly below the Union average in relation to GDP (under 5%). At the same time, only in Ireland was the share of spending on health care significantly higher than the Union average (around 28½% of the total), but this reflects a low level of overall spending rather than high expenditure on health (which was slightly below average in relation to GDP).

Spending on income transfers to the unemployed, which is often regarded as a primary cause of high levels of social spending, in practice, accounts for only a minor part of spending in all Member States. In 1995, it absorbed only 8% of the total social protection budget in the Union (under 2½% of GDP), the same as disability benefits and only a little

Table 1 — Division of current expenditure on social protection by function, 1995

	B	DK	D	E	F	IRL	I	L	NL	A	P	FIN	S	UK	E14
								% total expenditure							
Sickness	4.6	3.5	6.9	5.5	3.0	5.6	0.9	2.9	7.1	3.9	2.9	4.0	4.9	3.7	4.6
Health	19.6	13.8	22.9	23.7	24.4	28.3	19.6	20.6	20.4	20.9	26.3	16.7	16.5	21.2	21.8
Disability	6.1	10.3	6.7	7.5	5.6	4.5	6.9	12.7	14.7	7.5	10.7	14.4	12.1	11.4	8.0
Old-age and survivors	39.8	36.6	40.8	44.1	40.7	24.9	62.7	43.2	35.5	46.7	38.6	31.8	36.6	38.0	42.4
Family and children	7.7	12.0	7.2	1.8	8.5	11.2	3.4	12.8	4.4	11.0	5.1	12.9	11.2	8.7	7.3
Unemployment	13.4	14.3	8.8	13.9	7.8	16.6	2.1	2.9	9.6	5.4	4.9	13.9	11.0	5.7	8.1
Housing	0.0	2.4	0.6	0.4	3.0	2.9	0.0	0.2	1.0	0.3	0.0	1.5	3.4	6.8	1.9
Social exclusion	2.5	4.3	2.1	0.4	1.6	1.8	0.0	1.4	2.2	1.1	0.4	2.0	3.0	1.0	1.6
Administration	4.5	2.8	3.7	2.5	3.8	4.1	3.1	2.8	3.8	2.0	4.8	2.8	1.4	3.5	3.4
Other	1.8	0.0	0.2	0.3	1.5	0.1	1.5	0.6	1.3	1.3	6.3	0.0	0.0	0.0	0.8
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
								% GDP							
Sickness	1.4	1.2	2.0	1.2	0.9	1.1	0.2	0.7	2.2	1.2	0.6	1.3	1.7	1.0	1.3
Health	5.8	4.8	6.7	5.2	7.5	5.6	4.8	5.2	6.4	6.2	5.4	5.5	5.9	5.8	6.2
Disability	1.8	3.5	2.0	1.6	1.7	0.9	1.7	3.2	4.7	2.2	2.2	4.7	4.3	3.1	2.3
Old-age and survivors	11.8	12.6	12.0	9.6	12.5	5.0	15.4	10.9	11.2	13.9	8.0	10.4	13.0	10.4	12.1
Family and children	2.3	4.1	2.1	0.4	2.6	2.2	0.8	3.2	1.4	3.3	1.1	4.2	4.0	2.4	2.1
Unemployment	4.0	4.9	2.6	3.0	2.4	3.3	0.5	0.7	3.0	1.6	1.0	4.6	3.9	1.5	2.3
Housing	0.0	0.8	0.2	0.1	0.9	0.6	0.0	0.0	0.3	0.1	0.0	0.5	1.2	1.9	0.6
Social exclusion	0.7	1.5	0.6	0.1	0.5	0.4	0.0	0.4	0.7	0.3	0.1	0.7	1.1	0.3	0.5
Administration	1.3	1.0	1.1	0.6	1.2	0.8	0.8	0.7	1.2	0.6	1.0	0.9	0.5	1.0	1.0
Other	0.5	0.0	0.1	0.1	0.5	0.0	0.4	0.1	0.4	0.4	1.3	0.0	0.0	0.0	0.2
Total	29.7	34.3	29.4	21.8	30.6	19.9	24.6	25.3	31.6	29.7	20.7	32.8	35.6	27.3	28.5

Note: E14 excludes GR for which there is no breakdown by function

more than family allowances. Only in Belgium, Denmark, Finland, Sweden and Ireland did expenditure on unemployment benefits account for significantly more than 10% of the total and only in the first four of these did it amount to much above 3% of GDP (4–5% in each case). Moreover, of these four countries, only Finland had an unemployment rate above the Union average (over 16% as against just under 11%), the high spending in the other three being the result of relatively generous benefits levels combined with high rates of coverage (see Chapter 4).

As also mentioned above, however, spending on unemployment benefits as such covers only part of overall social expenditure on those out of work, which also, in practice, comes from disability benefits, housing allowances and social exclusion, as well as early retirement pensions (which, in principle, are included under unemployment benefits in the ESSPROS classification, but which are not separately distinguished from old-age pensions in some countries). In the Netherlands and the UK, in particular, as noted in Chapter 2 and elaborated in Chapter 4, disability benefits in the 1970s and 1980s became a means of providing long-term support to those unable to find a job, especially older workers, and, though the systems have been reformed of late, in 1995 they still accounted for a much higher share of social expenditure than unemployment benefits (50% higher in the Netherlands, almost twice as high in the UK).

Nevertheless, in relation to GDP, spending on disability benefits was equally high in the three Nordic countries — $3^1/_2$% of GDP in Denmark, around $4^1/_2$% in Finland and Sweden — where unemployment benefits were also higher than elsewhere. In these cases, this partly reflects the larger expenditure on benefits in kind than elsewhere — on the provision of social services — which was 3–4 times more than the Union average. This is also the case as regards family benefits, on which expenditure in the these Member States was twice as high relative to GDP than in the rest of the Union (around 4% in each case, with only Austria of the other Member States having a figure of over 3%) and for which benefits in kind represented around half of total spending in Den-

Table 2 — Growth of expenditure on social protection, 1990-95

% change per year

	B	DK	WG	D	GR	E	F	IRL	I	L	NL	A	P	FIN	S	UK	E13
Total expenditure on social protection																	
Expenditure in real terms (ie adjusted by GDP deflator)																	
1990-93	3.5	5.6	2.9	4.2	na	6.4	4.0	6.5	2.8	8.9	2.8	4.5	11.9	7.3	na	7.6	4.6
1993-95	3.5	0.5	2.8	2.9	3.4	-1.4	1.8	7.0	-0.2	4.2	-0.5	3.6	2.1	0.7	-0.5	2.0	1.6
1990-95	3.5	4.5	2.9	3.7	na	3.2	3.1	6.7	1.6	7.0	1.5	4.1	7.9	4.6	na	5.3	3.4
Change in relative prices (consumer prices relative to GDP deflator)																	
1990-93	-0.8	0.1	-0.1	0.0	na	-0.6	-0.1	-0.2	-0.3	1.1	0.9	0.0	-0.7	1.3	na	-0.9	-0.2
1993-95	0.0	0.1	0.2	0.1	0.4	0.2	0.2	1.7	0.4	-1.1	0.4	0.2	-0.7	-0.8	-0.7	0.7	0.2
1990-95	-0.5	0.1	0.1	0.0	na	-0.3	0.0	0.6	0.0	0.2	0.7	0.1	-0.7	0.4	na	-0.3	0.0
Expenditure in purchasing power terms (ie adjusted by consumer prices)																	
1990-93	4.4	5.5	2.9	4.2	na	7.1	4.1	6.7	3.0	7.7	1.9	4.4	12.7	5.9	na	8.6	4.8
1993-95	3.6	0.5	2.6	2.8	3.0	-1.6	1.6	5.2	-0.5	5.3	-0.9	3.4	2.9	1.5	0.2	1.3	1.4
1990-95	4.1	4.5	2.8	3.7	na	3.5	3.1	6.1	1.6	6.8	0.8	4.0	8.7	4.2	na	5.6	3.4
Expenditure, excluding unemployment benefits																	
Expenditure in real terms (ie adjusted by GDP deflator)																	
1990-93	3.3	5.3	2.6	3.8	na	5.1	3.7	5.6	2.6	8.9	2.5	4.1	11.1	3.5	na	7.0	4.1
1993-95	3.7	2.4	3	3.7	na	1.3	2.3	6.7	-0.1	4.0	-0.9	3.6	1.9	1.7	-0.2	2.7	2.3
1990-95	3.5	4.7	2.8	3.7	na	3.6	3.1	6.0	1.5	6.9	1.1	3.9	7.3	2.8	na	5.3	3.4
Change in relative prices (consumer prices relative to GDP deflator)																	
1990-93	-0.8	0.1	-0.1	0.0	na	-0.6	-0.1	-0.2	-0.3	1.1	0.9	0.0	-0.7	1.3	na	-0.9	-0.2
1993-95	0.0	0.1	0.2	0.1	na	0.2	0.2	1.7	0.4	-1.1	0.4	0.2	-0.7	-0.8	-0.7	0.7	0.2
1990-95	-0.5	0.1	0.1	0.0	na	-0.3	0.0	0.6	0.0	0.2	0.7	0.1	-0.7	0.4	na	-0.3	0.0
Expenditure in purchasing power terms (ie adjusted by consumer prices)																	
1990-93	4.2	5.2	2.7	3.8	na	5.7	3.7	5.7	2.8	7.7	1.6	4.1	11.9	2.2	na	8.0	4.3
1993-95	3.7	2.3	2.8	3.6	na	1.1	2.1	4.9	-0.5	5.2	-1.3	3.5	2.6	2.5	0.5	2.0	2.0
1990-95	4.0	4.6	2.7	3.7	na	3.8	3.1	5.4	1.5	6.7	0.4	3.8	8.1	2.3	na	5.6	3.4

Note: DK 1990-94 and 1994-95; GR, S no data before 1993; E13 excludes GR and S

mark and Sweden and over a third in Finland.

For the rest, expenditure on sickness benefits was around 1% of GDP or less in all countries except Sweden, where it was 1½%, and Germany and the Netherlands, where it was 2%, as was spending on housing in all countries except the UK (2% of GDP), reflecting its importance as an element in means-testing and the targeting of benefits on those in need (those receiving social transfers having all or part of their housing costs paid if household income falls below a minimum level). Spending on social exclusion was also relatively low in most countries, zero or close to zero in the Southern Member States and only over 1% of GDP in Denmark and Sweden — though in this case there may be classification problems, insofar as expenditure on ensuring that nobody's standard of living falls below a minimum level can potentially be met through other elements. Finally, administrative costs accounted for 5% or less of total social spending in 1995 in all countries (1% of GDP or less).

Growth of social expenditure

Total spending on social protection in the Union, taking the ESSPROS definition of gross expenditure, increased from just under

26% of GDP to 28½% over the five years 1990 to 1995. This compares with a rise of around 1% of GDP over the 1980s (on the previous ESSPROS system of classification). The increase was common to all Member States, with the sole exception of the Netherlands where there was a small fall. (As noted above, the change in net terms is likely to have been less.)

The rise, however, was confined to the period 1990 to 1993, the years of recession when there was very little growth at all in GDP in real terms (growth averaged only ½% a year over these three years). All of the Member States showed an increase over this period (leaving aside Greece and Sweden for which no data are available), especially Finland and the UK, where the recession was associated with a decline in GDP, though also Portugal, where, as noted below, spending rose particularly sharply.

In the two years 1993 to 1995, after the recession came to an end (growth averaging 2½% a year), expenditure on social protection in the Union declined slightly relative to GDP (by almost ½ percentage point). It rose only in Belgium, Germany, Greece and Austria, falling in all other Member States. The fall was particularly marked in the Netherlands (2 percentage points) and Sweden (3 percentage points), where the level of spending was among the highest in the Union, though it was also significant in Spain and Italy, where the level was comparatively low.

The increase in the underlying rate of GDP growth, however, was not the only reason for the difference in experience during the two parts of the period. Just as importantly, expenditure on social protection increased by considerably less in the last two years of the period than in the first three (indeed, expenditure would still have risen significantly relative to GDP across the Union between 1990 and 1993 even if GDP growth had been the same in the two sub-periods). In the three years 1990 to 1993, the real value of social spending to beneficiaries (ie adjusting for the increase in consumer prices) rose by an average of almost 5% a year in the Union, whereas in the subsequent two years, it went up by only 1½% a year (Graph 20).

The decline in real growth was especially marked in Spain, Portugal and the UK, where growth between 1990 and 1993 had been higher than in other Member States, at over 6% a year (over 12% in Portugal, though there are doubts about the figures) — a rate also reached in Ireland, where GDP increased by much more than elsewhere (by 3½% a year). Indeed in Spain, as well as in Italy and the Netherlands, the real value of expenditure declined over the two years 1993 to 1995, while in Sweden (for which no comparable data exist for the earlier period), it remained virtually unchanged (though it fell in terms of GDP prices as a whole instead of consumer prices, while in the former three countries, the fall was less in terms of GDP prices; see Table 2).

To some extent, this slowdown in expenditure growth is a consequence of the stabilisation of unemployment in 1994 and 1995 after the large rise which occurred during the recession years. Excluding unemployment benefits from the calculation reduces the difference in growth rates between the two sub-periods by around 1% a year on average (reducing growth in the first period by ½% a year and increasing it in the second by a similar amount). The reduction, however, was much more in Spain, where the number unemployed rose by over 40% between 1990 and 1993 and remained constant in the subsequent two years, and in Finland, where the number unemployed went up by almost 5-fold in the earlier period. In Spain, social spending excluding unemployment benefits rose by 1% a year in real terms between 1993 and 1995 instead of falling by 1½% and in Finland, it rose by 2% a year in the earlier period instead of by 6% and by 2½% a year after 1993 instead of by 1½%. For the latter country, therefore, the relative rates of spending growth are reversed if unemployment benefits are excluded.

Nevertheless, for most Member States, the effect on the pattern of social expenditure growth of differential changes in unemployment seems to be relatively small. This is largely because unemployment benefits *per se* represent a comparatively small element of spending on social protection, as noted above. On the other hand, there are other means of providing income support to the unemployed, as also noted above, and any full assessment of the implications of large numbers out of work for social spending has also to take account of these (in addition, of course, to the effects on finance of high unemployment).

Apart from unemployment benefits, old age pensions and health care showed the largest rise over the period (up by 1% of Union GDP and 1/2% respectively), in part reflecting the ageing of the population, though in the case of health care, spending fell relative to GDP in a number of countries between 1993 and 1995.

Means-testing

Although attempts have been made in most Member States to target social protection on those most in need, benefits subject to means-testing, one of the main ways of achieving this, still account for only a small proportion of spending across the Union. In 1995, they accounted for 11% of total expenditure on benefits in the Union, just under half of this comprising benefits in kind, especially in the form of assistance with housing and support for families with children, which together represented over two-thirds of this element.

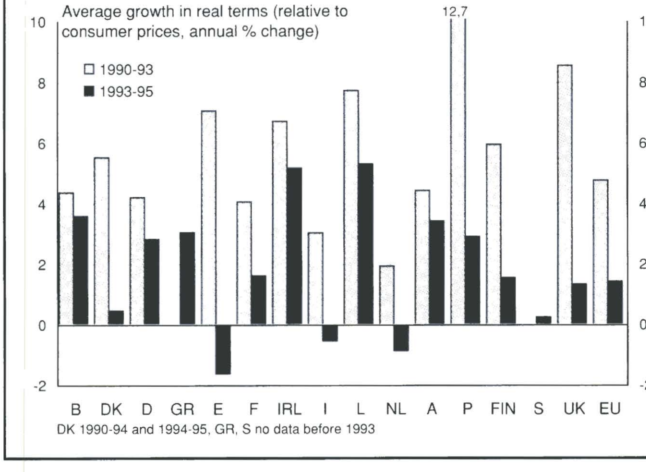
The scale of means-testing, however, varies significantly between Member States. It is most important in Ireland, where it accounted for 34% of overall spending on social benefits in 1995, and the UK, where it amounted to almost 23% of the total (Graph 21). In the rest of the Union, apart from Spain (and conceivably Greece, for which there are no data), where it accounted for 13 1/2% of the total, it represented less than 10% of overall spending in each Member State, though only marginally so in Germany and France.

There is also some difference in the division of means-tested benefits between cash transfers and benefits in kind. In Ireland and Spain, three-quarters of the spending was on the former, in the UK, more than half on the latter — indeed, cash benefits subject to means-testing accounted for as much of total transfers in Spain as in the UK. The significance of this distinction, however, is in some degree open to question, since in some countries, means-tested transfers might be set at a level to cover rent, for example, whereas in others it is covered directly.

The importance of means-testing, though relatively modest overall, is, nevertheless, tending to increase, though this is as much due to changes in underlying circumstances — in the rise in long-term unemployment, for example — as to changes in policy as such. In most Member States, its share in total spending went up between 1990 and 1995, the Netherlands, being the only country where the share declined. The rise was particularly marked in Finland (from 2 1/2% to 6 1/2%) and the UK (from just under 20% to just under 23%).

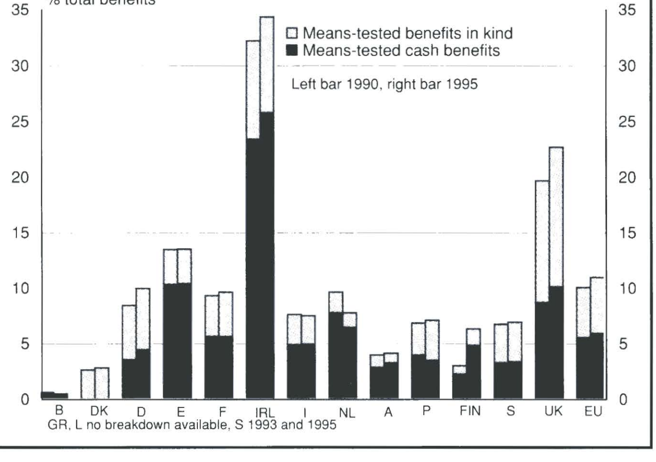
Indeed, means-testing now affects most broad areas of social protection in most countries, if only to a small extent. In the case of housing and social exclusion, most expenditure — all in the case of housing — was subject to means-testing in 1995 in all countries, though these together accounted for under 30% of total means-tested spending in the Union (but three-quarters in Sweden) (Table 3). Support for children and families accounted for over 20% of means-tested spending (this was the only element of spending which was

20 Growth of expenditure on social protection in real terms in Member States, 1990-95



DK 1990-94 and 1994-95, GR, S no data before 1993

21 Means-tested benefits in relation to total expenditure on benefits in Member States, 1990 and 1995



GR, L no breakdown available, S 1993 and 1995

Table 3 — Expenditure on means-tested benefits, 1990 and 1995

	B	DK	D	E	F	IRL	I	NL	A	P	FIN	S	UK
Family 1990													
% spending on family	0.0	2.0	29.5	14.5	23.8	34.9	36.4	13.3	1.5	25.3	1.8	0.1	48.9
% total means-tested spending	0.0	9.1	29.1	1.9	24.0	12.3	23.5	7.8	3.8	26.4	8.1	0.2	22.4
1995													
% spending on family	0.0	2.7	37.2	34.7	24.6	40.4	46.7	4.6	1.8	31.9	3.2	0.1	55.7
% total means-tested spending	0.0	11.9	28.2	4.7	23.0	13.8	22.0	2.8	5.0	26.0	6.7	0.1	22.0
Unemployed 1990													
% spending on unemployed	0.0	0.0	8.2	27.3	8.2	68.6	4.4	56.0	19.4	26.3	11.4	0.0	43.7
% total means-tested spending	0.0	0.0	9.5	31.9	7.3	31.0	1.0	48.6	22.3	9.7	23.4	0.0	12.7
1995													
% spending on unemployed	0.0	0.0	13.9	27.3	7.5	73.1	3.8	38.5	20.6	24.2	16.4	0.0	48.9
% total means-tested spending	0.0	0.0	12.7	29.0	6.4	36.9	1.1	50.2	27.8	18.9	37.2	0.0	12.7
Old-age 1990													
% spending on old-age	1.4	0.0	2.6	11.7	4.0	26.7	2.9	0.0	2.8	6.8	0.8	3.1	9.2
% total means-tested spending	100.0	0.0	13.7	38.4	18.3	25.4	22.5	0.1	35.1	43.1	9.1	17.2	20.0
1995													
% spending on old-age	1.0	0.0	2.5	11.1	3.1	25.1	2.2	0.0	3.1	5.7	1.1	2.6	10.5
% total means-tested spending	100.0	0.0	10.5	37.2	13.9	19.0	19.7	0.1	35.9	35.2	5.6	14.2	18.3
Housing 1990													
% spending on housing	0.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
% total means-tested spending	0.0	90.9	7.9	4.4	30.9	11.0	0.2	11.5	12.2	0.7	25.3	48.9	30.4
1995													
% spending on housing	0.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
% total means-tested spending	0.0	88.1	6.1	2.9	33.0	8.9	0.2	14.2	7.6	0.4	23.7	49.3	31.1
Social exclusion 1990													
% spending on social exclusion	0.0	0.0	90.0	97.5	39.0	92.7	0.0	100.0	68.5	78.8	46.5	51.4	100.0
% total means-tested spending	0.0	0.0	21.3	2.3	5.2	4.7	0.0	29.0	22.0	3.7	29.4	25.8	4.0
1995													
% spending on social exclusion	0.0	0.0	95.1	98.4	53.3	98.2	0.0	100.0	67.7	88.1	69.4	65.6	100.0
% total means-tested spending	0.0	0.0	21.2	3.1	9.4	5.3	0.0	29.5	19.0	5.2	23.0	29.0	4.5
Disability 1990													
% spending on disability	0.0	0.0	24.3	15.1	21.9	31.5	51.7	1.7	2.6	6.8	0.9	4.9	22.1
% total means-tested spending	0.0	0.0	18.2	8.9	14.3	4.4	52.3	2.9	4.5	16.4	4.8	7.9	10.0
1995													
% spending on disability	0.0	0.0	25.9	15.7	23.2	32.6	58.2	1.6	2.5	7.9	1.6	4.1	19.4
% total means-tested spending	0.0	0.0	18.1	8.9	14.2	4.5	55.9	3.1	4.6	13.3	3.7	7.3	10.2
Health care 1990													
% spending on health care	0.0	0.0	1.3	6.7	0.0	12.8	0.0	0.0	0.0	0.0	0.0	0.0	0.1
% total means-tested spending	0.0	0.0	3.7	12.2	0.0	11.2	0.0	0.0	0.0	0.1	0.0	0.0	0.2
1995													
% spending on health care	0.0	0.0	1.3	7.8	0.0	13.4	0.0	0.0	0.0	0.3	0.0	0.0	0.2
% total means-tested spending	0.0	0.0	3.2	14.1	0.0	11.6	0.0	0.0	0.0	1.1	0.0	0.0	0.1
Sickness 1990													
% spending on sickness	0.0	0.0	0.0	0.0	0.0	0.2	2.5	0.1	0.0	0.0	0.0	0.0	1.6
% total means-tested spending	0.0	0.0	0.0	0.0	0.0	0.0	0.5	0.1	0.0	0.0	0.0	0.0	0.5
1995													
% spending on sickness	0.0	0.0	0.0	0.0	0.0	0.2	10.3	0.1	0.0	0.0	0.0	0.0	6.8
% total means-tested spending	0.0	0.0	0.0	0.0	0.0	0.0	1.2	0.1	0.0	0.0	0.0	0.0	1.2

Note: GR, L no breakdown available; S 1993 and 1995 means-tested in Denmark) and around 40% of such support was subject to means-testing — up in all countries, except the Netherlands, between 1990 and 1995. Unemployment was a major element of means-tested expenditure in a number of Member States, being responsible for over a third of all such spending in Ireland, the Netherlands and Finland and for over a quarter in Spain and Austria, though only in Ireland (73%) and the UK (49%) was a substantial part of benefits subject to means-testing. Assistance to the elderly also represented an important part of overall means-tested spending in some countries, over a third of the total in Spain, Austria and Portugal, but in these countries as elsewhere, only a very small proportion of old-age benefits were means-tested (10% or less in most cases). In Ireland, however, the figure was as high as 25%.

Growth of spending by function, 1990–95

Although the continued expansion of spending on old-age pensions and health care was the main contributor to the growth of expenditure which has occurred over the 1990s, simply because these are the two largest elements of social protection, they were not the areas where the largest proportionate increase has taken place. Both housing and social exclusion showed average rises in spending in real terms (relative to consumer price inflation) of around 5% a year in the Union as a whole between 1990 and 1995, compared with 2½–3% growth in pensions and health care, though since one country, the UK, accounts for around half of all expenditure on housing benefits in the Union, the overall rise is dominated by what occurs in this country, which was somewhat out of line with developments elsewhere. (Real spending increased by 9% a year in the UK, reflecting in part the growing reliance on means-testing, but declined significantly in Spain, Italy, the Netherlands, Austria and Portugal.) By contrast, expenditure on social exclusion rose markedly in most Member States — the only exception being the Netherlands — reflecting not only the added weight given to combating this problem, but also the growing numbers not adequately covered by the 'core' elements of social protection (Table 4).

Growth in the latter was more than that of spending on unemployment benefits, despite the large increase in the numbers out of work which occurred over the period (though in Finland, where the biggest rise took place, and in Portugal, where spending was very small, expenditure rose sharply). The increase in expenditure on unemployment benefits, however, as noted above, was wholly concentrated in the recession in the first three years of the period, when it rose by 9% in real terms in the Union as a whole (and by over 40% in Finland and Portugal. In the two years 1993 to 1995, it fell significantly in real terms, as explored further below, with most countries, even those where the number out of work continued to rise, albeit at a slower rate, showing a decline.

The decline in real expenditure in the latter period was common to all elements of social protection, at least at the Union level, except sickness benefits, which rose only marginally in the earlier years, and social exclusion, where spending went up by much the same in both periods, with even administration costs rising only slightly after 1993 (though partly due to a large reduction in Italy, which was concentrated in 1995 and which may be a result of some reclassification of expenditure). Apart from social exclusion and housing (which, as noted above is dominated by events in the UK), only old-age pensions and disability benefits showed a growth of more than 2% a year between 1993 and 1995. The growth in spending on disability benefits, moreover, was due to a large extent to an expansion of almost 6% a year over this period in Germany (which accounts for almost half of the rise in the Union as a whole) and, to a lesser extent, to an increase of 4½% a year in the UK (since when, as noted in Chapter 2, the system has been tightened considerably).

Growth of spending on old-age, in contrast, continued in most Member States between 1993 and 1995 if at a lower rate than before, with only the Netherlands showing a fall, though only in Portugal (7½%), Luxembourg (4½%), Belgium and Germany (both 3½%) was it more than 3% a year and in Ireland, Sweden and the UK, growth was only around 1% a year. Expenditure on this item together with that on unemployment benefits is examined in more detail below, since for these elements at least there are indicators of the number of potential beneficiaries, if not the actual number.

Table 4 — Growth of social expenditure by function in purchasing power terms, 1990-95

% change per year

	B	DK	WG	D	E	F	IRL	I	L	NL	A	P	FIN	S	UK	E13
Sickness																
1990-93	0.4	-3.4	0.4	1.3	8.2	0.5	1.6	-5.1	8.3	-2.1	2.0	1.0	-7.2	na	-1.3	0.3
1993-95	0.2	21.0	2.8	3.4	-0.9	-1.7	16.5	-9.5	3.5	-8.2	0.3	8.4	0.2	-10.4	-2.4	0.3
1990-95	0.4	1.0	1.4	2.2	4.5	-0.4	7.3	-6.9	7.0	-4.6	1.3	3.9	-4.3	na	-1.7	0.3
Health																
1990-93	7.1	3.4	3.3	4.2	5.8	3.7	8.5	0.0	8.3	5.9	4.5	18.7	-2.0	na	8.4	4.1
1993-95	1.5	-2.1	4.5	4.6	0.4	2.1	5.0	-4.9	7.0	0.7	3.4	2.0	0.6	0.9	3.2	1.8
1990-95	3.7	2.3	3.7	4.3	3.6	3.0	7.1	-2.0	8.0	3.8	4.0	11.8	-0.9	na	6.3	3.2
Disability																
1990-93	-0.3	6.0	5.9	7.0	4.6	1.8	5.6	1.6	4.8	0.1	4.1	6.3	5.9	na	17.4	5.6
1993-95	1.9	5.9	3.1	5.8	0.1	3.0	9.4	-1.5	12.3	-1.3	9.0	-3.5	0.7	7.2	4.4	2.8
1990-95	0.6	6.0	4.7	6.5	2.8	2.3	7.1	0.3	6.7	-0.4	6.0	2.3	3.8	na	12.0	4.5
Old-age and survivors																
1990-93	5.5	5.8	1.9	2.8	5.2	3.6	3.7	4.8	7.5	1.8	3.4	10.3	4.2	na	6.3	4.1
1993-95	3.5	2.1	1.9	3.6	2.7	2.3	1.2	2.0	9.5	-0.7	3.0	7.6	2.4	0.9	0.9	2.4
1990-95	4.7	5.0	1.9	3.1	4.2	3.1	2.7	3.7	8.0	0.8	3.2	9.2	3.5	na	4.1	3.4
Family and children																
1990-93	1.2	6.4	4.3	4.6	6.2	2.6	6.2	-5.8	12.6	-2.8	7.2	6.9	2.3	na	8.2	3.3
1993-95	0.3	1.0	0.0	-1.1	1.8	1.4	7.7	-3.3	19.1	-3.1	3.5	1.1	6.6	-1.6	2.1	0.5
1990-95	0.9	5.3	2.5	2.3	4.4	2.1	6.8	-4.8	14.2	-2.9	5.7	4.5	4.0	na	5.7	2.2
Unemployment																
1990-93	5.3	7.2	7.0	8.4	14.0	7.6	12.4	14.3	9.0	5.5	11.9	42.2	46.5	na	17.5	10.4
1993-95	2.8	-9.5	0.2	-4.8	-14.5	-4.1	6.4	-4.1	22.1	3.4	2.7	8.6	-3.9	-1.5	-8.3	-5.3
1990-95	4.3	3.6	4.2	3.0	1.6	2.8	9.9	6.5	12.2	4.6	8.2	27.7	23.7	na	6.4	3.9
Housing																
1990-93	0.0	6.6	-1.7	9.4	-0.7	5.8	2.1	-3.1	3.4	0.0	-7.6	-11.8	21.9	na	12.5	8.9
1993-95	0.0	0.7	5.9	-7.5	-10.5	3.7	4.8	-5.3	2.6	1.7	0.0	7.1	16.3	2.1	4.6	2.7
1990-95	0.0	5.4	1.3	2.3	-4.8	5.0	3.1	-4.0	3.2	0.7	-4.6	-4.6	19.6	na	9.3	6.4
Social exclusion																
1990-93	24.4	9.8	4.7	4.0	18.3	10.6	10.6	10.9	4.9	-2.9	8.9	26.6	9.7	na	16.3	7.2
1993-95	4.6	3.7	9.5	10.7	-1.3	8.4	7.2	12.4	8.4	-3.5	-7.6	-0.5	1.8	-4.6	4.6	6.4
1990-95	16.1	8.6	6.6	6.6	10.0	9.7	9.2	11.5	6.3	-3.1	1.9	14.9	6.5	na	11.5	6.9

Note: Growth is measured in relation to consumer price inflation; B 1990-92 and 1992-95 for health; DK 1990-94 and 1994-95; GR no data; S no data before 1993; E13 excludes GR and S

Growth in old-age pensions

As yet the ESSPROS data do not include figures of the number of people receiving old-age pensions or other kinds of benefit (though a module is planned for these in the future), which would make it possible to examine the average amount received and to distinguish the effect on expenditure of the changing numbers of recipients from that of changes in the average level of benefit. Some estimates, however, can be made of the potential numbers drawing old-age pensions from demographic data, which indicate for each Member State, the numbers above the official age of retirement. These can be combined with Labour Force Survey data on those retiring before they reach this age to give an estimate of the total number who might be eligible to receive a pension. (Although early retirement for labour market reasons is, in principle, included under unemployment benefit, in practice, about half the Member States include nothing under this head and in the others, only part of such retirement is for labour market reasons.) This, of course, may differ significantly from the number who are actually in receipt, which will depend on the regulations in force in the country in question. Because of this, the estimates produced by this kind of exercise give at best a very approximate indication of average benefit levels and how these are tending to change over time. (Data from the ECHP, which are based on what people actually receive, should give a better guide to pension levels; these data are examined in Chapter 7 below.)

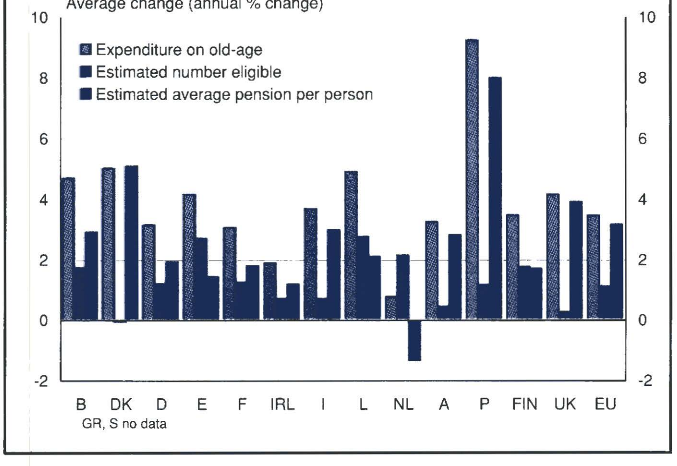
Nevertheless, at present, though unsatisfactory, they are the only means of assessing the relative importance of the main factors underlying changes in expenditure. Between 1990 and 1995, the number of people above official retirement age in the Union (which differs between Member States) increased by just under 1% a year, though the rise varied from over 2% a year in Belgium and Spain (where it was almost 3%) to under 1/2% a year in Denmark, Austria, Sweden and the UK. Growth of the elderly population was also relatively high in Italy, though here the potential effect on expenditure was moderated by an increase in the official retirement age (from 60 to 62 for men and from 55 to 57 for women) over the period. As a result, the number above this age declined. This, however, was accompanied by a significant increase in early retirement, which offset much of the effect of the rise in the official retirement age (in practice, the increase in the latter was not matched by an equivalent rise in the actual age at which people retired).

Elsewhere the continuing reduction in the effective age of retirement, despite a shift in government policy in the opposite direction, reinforced demographic trends and added to the growth in the number potentially eligible for an old-age pension — to just over 1% a year in the Union as a whole. In consequence, around 30% of the overall increase in expenditure on pensions can be attributed to the growth in the number of potential recipients, implying a rise of some 2 1/2% a year between 1990 and 1995 in the average value of pensions. The growth in the latter and its contribution to the increase in real spending relative to that in the number of potential recipients, however, varies markedly between Member States. In Spain, where expenditure growth was above the Union average, the increase in estimated numbers explains most of the rise, as it does in the Netherlands and Finland (Graph 22). Indeed, in Spain, the increase in the average pension was only around half of that in the rest of the Union, while in the Netherlands, the average pension seems to have declined by over 1% a year in real terms. On the other hand, in Denmark and Portugal, where the growth of spending was also well above the Union average, the number of potential recipients hardly changed at all in the former and rose by no more than in other countries in the latter, implying a substantial increase in the average pension in both cases.

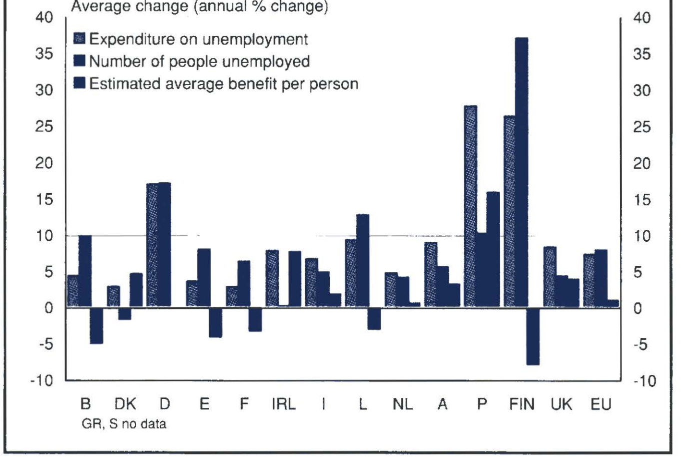
Growth in unemployment benefits

A similar division between changes in the number of people qualifying for social support and the average amount paid can also be made in respect of unemployment

22 Change in expenditure on old-age pensions and estimated number of people eligible, 1990-95



23 Change in expenditure on unemployment and number of unemployed, 1990-95



benefits, in this case based on those classified as being unemployed according to the internationally-accepted definition (those available for work and actively seeking it). This definition, however, differs from that used to determine eligibility for benefit in Member States, each of which has a slightly different method and, even more than in the case of pensions, therefore, estimates of benefit recipients might diverge significantly from the actual number in receipt, though the divergence is likely to be less as regards changes over time.

In the Union as a whole, the number unemployed increased by 8% a year over the 5 years 1990 to 1995, about the same as the rise in real expenditure on unemployment benefits. The average amount paid per person unemployed, therefore, appears to have remained much the same in real terms over this period. In 5 Member States, however — Belgium, Spain, France, Luxembourg and Finland — the average benefit seems to have declined, especially in Finland, where the growth in real expenditure was higher than in all Member States, but where the number unemployed also increased by much more than anywhere else (Graph 23). In Denmark, Ireland and, above all, Portugal, in contrast, average benefit is estimated to have risen markedly (in Portugal, by over 15% a year).

These estimates, however, could reflect not only the divergence of national definitions of unemployment from the international convention but also changes in coverage as much as changes in average benefit levels. This is especially the case in countries, such as Spain, Italy and Portugal, where a minority of the unemployed, even on national definitions, qualify for benefit (see Chapter 4 below). A change in coverage, moreover, need not necessarily be a result of a change in the conditions governing entitlement to benefit. It could equally result from a change in the characteristics of the unemployed, in particular from an increase in the proportion who have been out of work for a long period of time, who tend in many countries to receive less than those joining the register more recently. Nevertheless, it is evident from Chapter 2 above and Chapter 4 below, that the criteria for eligibility for benefit were tightened in most Member States between 1990 and 1995, in addition to a reduction in benefit levels in some cases, and this is reflected in the falls or modest rises in estimated average payments in real terms in the majority of countries (only 6 Member States showing an increase in the latter of more than 1% a year over this period).

Sources of funding

The finance for systems of social protection in all Member States comes partly from social contributions, levied mostly on income from employment and divided between employers and those being protected (ie employees and the self-employed), and partly from general taxation. In a number of countries, however, as mentioned above, contributions are also levied on benefit recipients. Moreover, in some Member States, 'earmarked' taxes have been introduced in recent years (in Belgium, France and Luxembourg, in particular), with the aim largely of shifting the cost from employment to the population in general, or to specific sections of it, such as consumers of energy. The same aim has been common to most Member States, the concern being to reduce contributions levied on employers, which may add to labour costs and so both discourage job creation and adversely affect competitiveness, compensating for this by raising either employees' contributions or taxes, though not necessarily earmarked ones.

Nevertheless, according to the new ESSPROS data, just under 40% of finance for social protection in the Union still came from contributions levied on employers in 1995, a further 24% or so from contributions paid by those protected (mainly employees, the self-employed and benefit recipients accounting for under 5% of total revenue) and most of the rest from general taxation (some 30%), with earmarked taxes accounting for under 2%. (It should be emphasised in this context that employers' contributions include voluntary amounts paid to fund social benefits granted to their employees as well as statutory amounts imposed by government — see Notes and sources.)

Although these different sources of finance are common to all Member States, their relative weight varies, largely reflecting the historical development of the social protection system itself. In most of the countries where the system has its origins in the provision of social insurance for those in employment (the so-called Bismarkian system) — the Benelux countries, France, Germany and Austria — social contributions still accounted for around two-thirds or more of funding in 1995 (as much as 77% in France, though only 63% in Austria), except in Luxembourg (where the data available show a share of only just over half). Within this, charges on employers are responsible for the largest share, except in the Netherlands (where their share of total funding amounted to 22% as compared with just over 49% in France, almost 15% of GDP) (Graph 24).

In the Nordic countries, the UK and Ireland, where the system has its origins in the provision of social welfare for those in need (the so-called Beveridge system), social contributions accounted for less than half of total finance in 1995 (40% or less in the UK and Ireland and only 23½% in Denmark), with employers again responsible for most of the finance raised by this means in all of the countries. Indeed, in Sweden, they provided almost 40% of total revenue for social protection and in Finland, 35%, much the same as in Austria and only slightly less than in Germany. Moreover, in relation to GDP, social charges on employers in Sweden were the same as in France and higher than in any other Member State, while in Finland, they were higher than in Germany.

In the South of the Union, in Spain and Italy (there are no data for Greece), the financing system is similar to that in the Bismarkian countries, with just over two-thirds of revenue coming from social contributions, again mostly from charges on employers. Indeed, in Spain and Italy, around half of all funding for social protection comes from the latter. In Portugal, on the other hand, the pattern of funding is more similar to that in the other Northern Member States, with just under half of revenue coming from contributions and those on employers accounting for 30% of all finance for social protection.

In line with stated policy aims, there is evidence of some shift in funding from contributions levied on employers to other sources over the 1990s. Between 1990 and 1995, the share of revenue raised from employers' contributions declined from 42% to 39½% in the Union as a whole. At the same time, the share raised from contributions from employees and other people protected increased from just over 22% to 23½%, while, more significantly, revenue from taxation rose from 29½% of the total to 32% (there was some fall in the share raised from other sources). This shift in funding sources was common to all Member States, except Denmark and the Netherlands, where employers' contributions are relatively small, and Belgium. It was especially marked in Portugal and Finland, where revenue from employers' contributions was reduced by some 20% in relative terms.

The shift, however, was concentrated in the first three years of the period, in the recession years between 1990 and 1993. In the two years 1993 to 1995, the share of revenue from employers' contributions in the Union as whole increased rather than declined, even if only slightly. Leaving aside Denmark and the Netherlands, where the employers' share rose throughout the period, this pattern of change was common to most countries in the Union, including Finland, where the marked fall noted above occurred in the first three years of the period, since when the share has edged up (though the fall in Portugal continued after 1993, it was much less than before). The only exceptions were France, Ireland, Luxembourg and Sweden, where the share of employers's contributions continued to decline after 1993.

At the same time, the share of revenue from employees' contributions also went up over the latter period, so that the share from taxation fell (from almost 33% to 32%), though within this, there was a continued rise in the importance of earmarked taxes, especially in France, where their share of total revenue rose from just under 6% in 1993 to almost 8% in 1995, having been only 3½% in 1990.

In general, therefore, the stated policy objective of shifting the funding of social protection from employers to other sources was not in evidence in the two years 1993 to 1995. Moreover, even in the previous three years when the revenue raised from charges on employers fell relative to that from other sources, this does not appear to have been translated into a reduction in the costs falling on employers, which is the main aim of policy (though it should be reiterated that part of the costs are voluntary rather than statutory; over the period 1990 to 1995, there was some tendency for the voluntary — or imputed — element to increase in relative importance). During this period, employers' contributions increased in most Member States in relation both to GDP and, more relevantly given the concern of relieving the cost falling on employment, to the overall wage bill (the share of which in GDP rose marginally between 1990 and

1993 but fell in the subsequent two years with economic recovery).

In the Union as a whole, revenue from employers' contributions rose marginally in relation to the overall wage bill (as measured by the compensation of employees) over the three years 1990 to 1993, despite the fall in its share of total receipts, and only in Germany, Luxembourg (both marginally) and Portugal, did it decline (Graph 25). Even in Finland, where it fell markedly as a share of total receipts, it increased relative to total labour costs. Between 1993 and 1995, revenue from employers rose by slightly more across the Union in relation to labour costs, from 22% of the wage bill to 22½%, with only Spain, Ireland, Luxembourg and Sweden registering a decline.

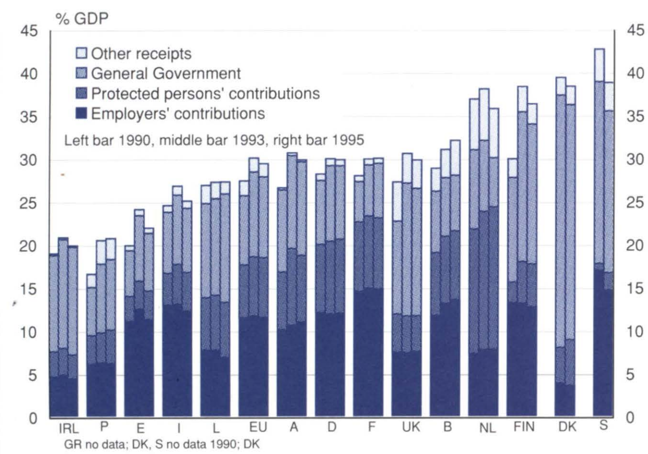
The funding obtained from employees' contributions increased by even more in relation to labour costs over the 5 years as a whole. In this case, the rise occurred more evenly over the period, with the three Nordic countries as well as the Netherlands showing a particularly marked increase, reflecting in Sweden a direct shift from employers to employees between 1993 and 1995. In Ireland and the UK, on the other hand, there was a slight fall as funding was shifted to general taxation.

The increase in employees' contributions was accompanied by an expansion of contributions levied on old-age pensioners and other benefit recipients, which reflects both a growing recognition of the increasing prosperity of pensioners as a group — though not of all individuals — and a desire to spread the cost of financing more evenly across the population. In most countries where these are levied, their share of total funding increased between 1990 and 1995, especially in the later years of the period, especially in the Netherlands and Germany. Nevertheless, they are levied in only 8 Member States and only in the latter two countries are they a significant source of funding (accounting for 8½% of the total in the Netherlands and 4% in Germany). At the same time, it should be recalled, as noted at the outset, that taxes imposed on benefit recipients are also a source of revenue in both these two countries and the three Nordic Member States, though, in most cases, they are not earmarked for social expenditure and are not separately distinguished in the ESSPROS data.

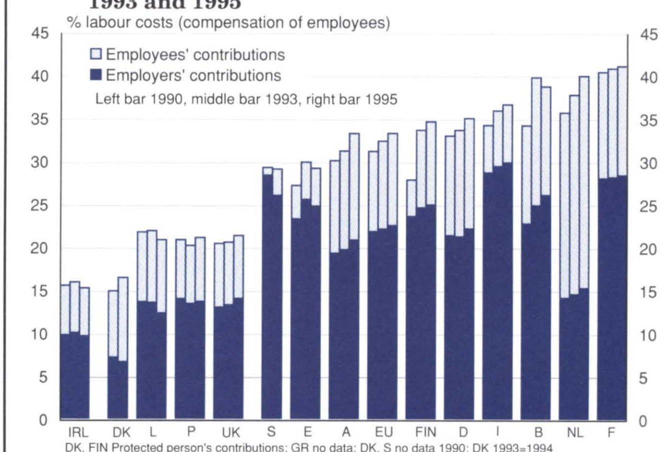
Total receipts relative to expenditure

The cost of social protection was examined earlier in this chapter in terms of expenditure on social transfers and other outlays. It is, however, equally relevant to consider the issue in terms of the revenue raised to fund social spending, since this will determine the taxes or contributions which individuals and companies need to pay. If revenue were set to match expenditure, then, of course, the matter would not arise, but, in practice, for a number of Member States there is a significant difference between the two. In most cases, receipts exceed expenditure, reflecting, in particular, the accumu-

24 Financing of social protection expenditure by source in Member States, 1990, 1993 and 1995



25 Employers' and employees' contributions in relation to labour costs in Member States, 1990, 1993 and 1995



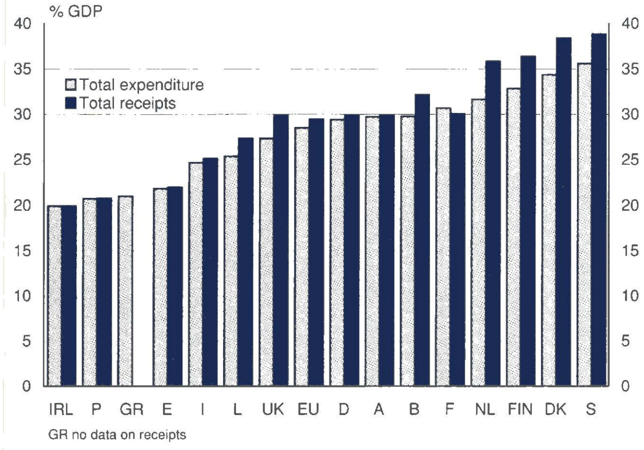
lation of reserves to cover both unexpected contingencies, such as increased demands on the system resulting from economic recession, and projected liabilities, such as future pension commitments. By contrast, in a few cases, receipts fall short of expenditure giving rise to a deficit covered initially by borrowing but implying a possible need for increased taxes and/or contributions in future years.

Over the Union as a whole, the funding raised for social protection in 1995 was around 1% of GDP higher than the expenditure incurred (ie some 29½% of GDP as against 28½%), and much the same was the case in earlier years (no data on revenue are at the time of writing available for Greece). In France, expenditure exceeded receipts, as it had done in each year since 1992, and there was consequently a deficit on social protection spending (which reached 1% of GDP in 1993). In four other Member States, Spain, Ireland, Austria and Portugal, receipts broadly matched expenditure, which again was true for earlier years, though in Portugal, there was a small deficit in both 1993 and 1994 (of around ½% of GDP).

In the rest of the Union, receipts exceeded expenditure in 1995, as also in earlier years, most markedly in Belgium, the Netherlands, the UK and the three Nordic countries, at between 2½% (in the UK) and just over 4% of GDP (in the Netherlands) (Graph 26). In each case, the gap was similar in the earlier years of the decade, even during the worst of the recession when the tax base was depressed and the demand for added spending relatively high. It would, therefore, appear that in these countries, at least, sizeable reserves are being built up to meet possible future liabilities, despite the fact that in most cases, only part of social expenditure is funded rather than pay-as-you go.

These significant differences in revenue relative to expenditure mean that a slightly different picture emerges of the cost of social protection in Member States if the former rather than the latter is taken as the basis of comparison. In particular, the level of costs (gross rather than net, ie again ignoring the taxes and contributions levied on benefits, as well as tax expenditures) in the three Nordic countries together with the Netherlands is even higher than in other Member States in terms of revenue than in terms of expenditure. Accordingly, there is a distinct gap between these four countries, where the lowest level of funding amounted to 35½% of GDP in 1995 (in the Netherlands) and the rest of the Union, where the next highest proportion was 32%, in Belgium, though around 30% in Germany, France, Austria and the UK. Moreover, whereas expenditure on social protection in the UK is significantly lower in relation to GDP than in any of these countries, the revenue raised to fund it is much the same. There is an even larger gap between these countries and Spain, Portugal and Ireland, where revenue was only around 20% of GDP (22% in Spain), with Italy and Luxembourg in between.

26 Total social protection expenditure and receipts in relation to GDP in Member States, 1995



Part 2 The incidence of social transfers

A major objective of systems of social protection is to relieve poverty, alleviate deprivation and reduce the most extreme disparities in the distribution of income. This is by no means the only set of objectives. Social protection is equally intended to provide a replacement income to those unable to work, because, for example, of sickness or inability to find a job, or who have reached the end of their working careers and to provide access to health care and other basic services to those who need them rather than simply to those who can afford to pay. Ensuring that people do not have to live on unacceptably low levels of income, however, is usually regarded as the central aim. It has historically been the motivating force behind the development of the arrangements now in place across the Union and tends to be how systems are judged. Moreover, with the tight constraints on social expenditure evident in all Member States, which are being accompanied by greater efforts to target spending on those most in need, it is one which is of growing importance and of increasing relevance to both the assessment and formulation of policy.

At the same time, assessing the effect of social protection in these terms is by no means straightforward. Even leaving aside data problems, there is a lack of agreement on what constitutes an unacceptable level of income and how much is needed to avoid poverty and deprivation. The intention here is to set definitional issues to one side for the most part and to focus mainly on the incidence

The Household Panel data used in the analysis

The data used in this section come from the first wave of the European Community Household Panel (ECHP) conducted in 1994, which covered all Member States except Austria, Finland and Sweden, these three consequently being excluded from the analysis. The data relate to household income in 1993 and to the various sources from which this arises, including the different kinds of social transfer. Income is measured in terms of purchasing power standards (PPS) to adjust for differences in price levels between Member States — ie in the purchasing power of a given unit of currency — as well as converting to a common currency (for the Union as a whole, PPS values are equivalent to ECU values). It includes income received from all sources, including from capital as well as employment and social protection schemes, but also transfers between households. The latter item gives rise to a minor inconsistency insofar as receipts of private transfers are included but not payments of these, though they are very small, amounting to only around 1% of income overall. Moreover, since they are slightly more important for poorer households than richer ones (amounting to around 2½% of total income for households with under half average income in the Union), they serve to give a more complete estimate of the income of these.

Households are converted to an equivalent basis by adjusting for differences in size and composition (specifically, by attaching the following weights to each member — 1.0 to heads of household, 0.5 to each additional adult and 0.3 to every child under 16), so as to allow for economies in purchases of goods and services.

All income — ie both the total and each individual component — is measured net of all direct taxes and social charges (but not indirect taxes). For France, however, where taxes are assessed on total income on an annual basis rather than being deducted at source, only total income is measured net of estimated taxes and income from different sources is measured gross of tax, though net of social contributions which are deducted at source. The figures for social transfers are, therefore, not strictly comparable with those for other countries, to the extent that they include an element of tax payable on these, even though this is relatively small. The effect is to overstate their value slightly relative to total household income, which is measured in net terms (by perhaps 1–2 percentage points), and this needs to be taken into account when interpreting the comparisons presented in the text.

Social transfers cover all cash benefits and allowances received by households, including private pensions, but exclude benefits in kind, such as health care (though they include housing benefits paid as cash, which are classified by ESSPROS as benefits in kind).

of social transfers on those with different levels of income, to examine their effect in lifting the income of those who would have little or nothing without it and in narrowing the gap between the poorest in society and the rest. As such, the analysis indicates how far social protection across the Union is targeted on those who appear to be most in need of support, and so by implication it bears on the issue of poverty and deprivation.

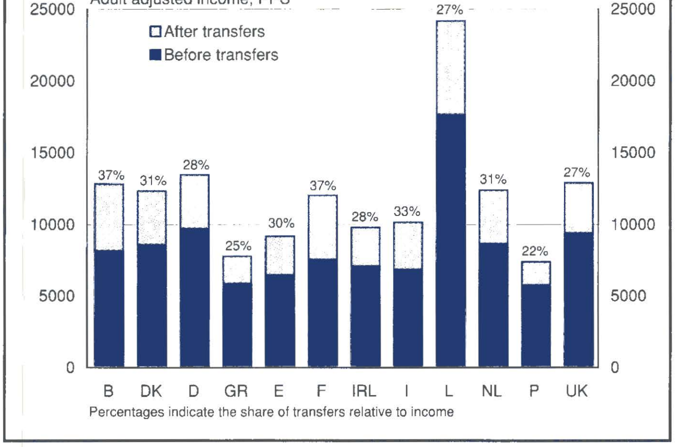
The analysis is based on the results of the first wave of the new European Community Household Panel (ECHP) carried out in 1994 which provides details of both the income received by individuals and households in 1993 and the different sources from which this arises (see Box). These data for the first time enable the scale of social transfers and their distributional incidence to be analysed on a comparable basis for all the Member States covered (all except Austria, Finland and Sweden). It should be emphasised, however, that though the data have been subject to a thorough process of checking and verification, because of the innovatory nature of the survey itself and the inherent difficulties in collecting reliable information on income, the findings are inevitably subject to a measure of uncertainty. This should become less as results from the second and third waves (conducted in 1995 and 1996) are processed and data from the first wave can be checked against these, which will happen during 1998. Until then, the results presented below should be regarded as tentative, though they ought to give a reasonable indication of the true situation.

The analysis is conducted in terms of households, which are the ultimate focus of systems of social protection and the most relevant basis of assessment given the economies achieved by people living together and given also the fact that certain benefits, particularly means-tested ones, apply to households rather than individuals. These are standardised to adjust for differences in size and composition (ie the number of people living in them and how many of them are children rather than adults), both of which affect the effective value of a given amount of income (see Box). All sources of income are taken into account, except benefits in kind, and income is measured net of direct taxes and social contributions so indicating the amount that households have available to spend.

The scale of social transfers

Social benefits account for a significant part of household income in all Member States. Social transfers, defined to include private pensions, represented around 30% of net household income in the Union in 1993 (excluding Austria, Finland and Sweden, as noted above). Their importance, however, varied markedly between countries from around 37% of net income in Belgium and France (though for the latter this figure is likely to be overstated, even if only slightly, by the fact that transfers include direct taxes not deducted at source — see Box) to 25% in Greece and only 22% in Portugal (Graph 27).

27 Average household net income in Member States, 1993



Percentages indicate the share of transfers relative to income

28 Households with transfers as the main source of income in Member States, 1993

In between, the share in Italy, the Netherlands, Denmark and Spain was between 30% and 33%, in Germany, Ireland, the UK, and Luxembourg, 27–28%.

The pattern of variation between Member States in these figures differs somewhat from that for expenditure on social protection examined in the previous section. In particular, the relative scale of social transfers in both Belgium and Italy is higher than indicated by the social expenditure figures, as it is in Ireland, where the latter figures are substantially lower, relative to GDP, than in the UK or Germany. These differences reflect a number of factors, not least the exclusion of benefits in kind (which, for example, are low in Italy), the inclusion of all private pensions and the difference between net household income and GDP (which is significant for Ireland, in particular, where some 13–14% of income goes abroad reflecting the importance of multinational companies in the economy). They also reflect the fact that transfers are measured net of taxes and other charges in the ECHP data but inclusive of these in the expenditure data, a difference which, as noted in the previous section, tends to reduce the gap in expenditure levels between countries (especially between Denmark and the other Member States).

Transfers as a source of income

The variation in the scale of social transfers across the Union is reflected in their importance as a source of household income, though this is also affected by the extent to which they are concentrated on households with relatively little income from other sources and the relative numbers of these. In the Union as a whole, social transfers were the main source of income for some 37% of households in 1993. In Belgium and France, as might be expected from their scale, social transfers represented the main source of income for a larger proportion of households than in the rest of the Union, over 40%, in each case (Graph 28). The figure for Ireland and the UK, however, where the scale of transfers was much less, was only slightly lower, reflecting the relatively uneven distribution of income before transfers, as noted below, and the correspondingly large number of households which are reliant on transfers to bring their income up to a reasonable level. In both cases, transfers were the main income source for proportionately more households than in Denmark or the Netherlands, where the overall amount transferred was much larger but where the pre-transfer distribution of income was more even.

The large number of households in the Union which appear to be dependent on social transfers reflects to a major extent, the relatively large number of people above retirement age. In 1993, the main source of income for some 28% of households was old-age pensions (including those paid to widows or widowers and from private as well as state schemes), higher than the proportion of the population above retirement age, partly because of the significant numbers retiring early, partly because of elderly people tending to live in smaller households, often alone. The fact that both of these factors vary between Member States, together with differences in the relative importance of other sources of income, leads to considerable variation in the proportion of households for which pensions are the main means of support. In Italy, where the relative number of people in retirement is higher than in other Member States, old-age pensions were the main source of income for around 34% of all households as opposed to only 23% in Ireland, where the proportion above retirement age is lower than anywhere else, and Denmark, where it is much the same as the Union average.

The variation in the importance of transfers other than pensions is even wider, though some caution needs to be exercised in attaching too much significance to such a division, since in some countries the support of those in retirement might come wholly from pensions, in others from other kinds of benefit as well. In Ireland, transfers other than pensions are the main income source for just under 18% of households, in Denmark for 13%. In the former, this partly reflects the high level of unemployment in 1993 (15½%), in the latter, the relative scale of a range of benefits, including for sickness, disability and family support as well as unemployment. A similar proportion of households in the UK were dependent on other transfers as in Denmark, though, since the relative amount transferred was much less, as indicated below, this again reflects the comparatively large number of households with little or no income from other sources (many consisting of only one person of working age as indicated in Chapter 1).

By contrast, very few households in Greece and Italy obtained most of their income from transfers other than pensions — only 1½% and 3½%, respectively — reflecting the limited extent of social benefits available in both countries (though there may be a classification problem in the way that some transfers are recorded in the ECHP, such as the *Cassa Integrazione Guadagni* in Italy, under which transfers are made to companies which then pass these on to workers on lay-off).

The composition of transfers

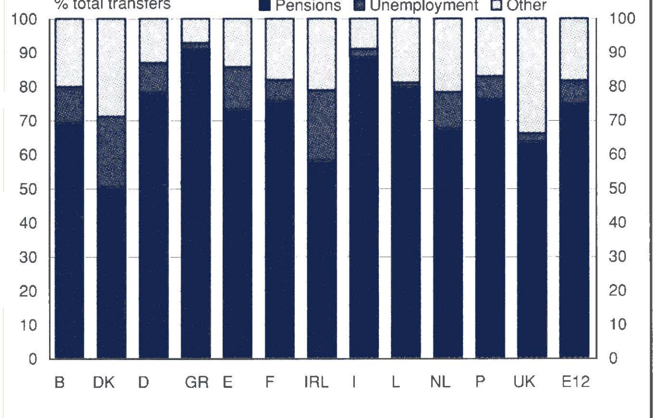
As implied above, old-age pensions are the largest element of transfers in all Member States, representing an average of 75% of the total in the Union in 1993. In Denmark, however, they accounted for only just over 50%, whereas in Italy and Greece, they accounted for around 90% and in Luxembourg and Germany, almost 80% (Graph 29). Elsewhere, they represented around 70–75% of the amount transferred except in Ireland and the UK, where the figure was around 60%.

Of the other transfers, unemployment benefits accounted for 20% of the total in Denmark and Ireland, and just over 10% in Spain, Belgium and the Netherlands, but for less than 3% in Italy, Greece and Luxembourg as well as the UK.

For the first three of the latter four countries, the small amount involved is understandable in view of the low rate of unemployment in Luxembourg and the nature of the unemployment compensation system in Italy and Greece. For the UK, on the other hand, where the system is similar to that in Ireland and where unemployment was around the Union average in 1993, it suggests that a large part of transfers to the unemployed are classified under a different head, specifically as social assistance (this seems to be confirmed by the relatively large amount of such transfers recorded by the ECHP).

For the rest, the figures are broadly in line with the ESSPROS data analysed above, so that, for example, disability and sickness benefits are relatively important in the Netherlands, the UK and Denmark, while family benefits are more significant in Belgium and Ireland.

29 Composition of social transfers in Member States, 1993



The effect of transfers on household income

While the data compiled by the ECHP should give reasonable estimates of net, or disposable, household income, they do not provide a reliable indication of gross income before any taxes or charges are deducted (because these are mostly deducted at source, people often have only a vague idea of their gross earnings). Consequently, it is not possible to analyse the combined effect on the distribution of income between households of the tax and benefit systems, but only the effect of transfers in relation to income after direct taxes and social contributions have been deducted. The approach adopted below is to begin by examining the distribution of household income in each Member State before social transfers (by deducting the latter from reported income) — to identify the *ex ante* position — and then to compare this with the distribution which actually prevails after transfers are made.

This, of course, provides only a partial indication of the extent of income redistribution brought about by government. Since, however, the main concern here is with the distribution of social transfers between households, rather than with the effect of the fiscal system as such, the lack of data on gross income is not so much of a problem, though it prevents an analysis of the way in which the financing of social transfers is distributed between income groups. It should also be noted that since the distribution of income tends to change only very slowly over time, because of the rigidities built into it (people tend to stay in the same job for fairly long periods of time, for example and, therefore, have much the same relative level of earnings year after year), the position in 1993, to which the ECHP data relate, is unlikely to be very different from that in 1997 or 1998.

Income distribution before transfers

The distribution of income between households before social transfers does not vary a great deal between Member States. This can be shown in a number of different ways. A standard graphical means is through what are known as Lorenz curves, which show the proportion of total households in a country (ranked according to their income along the vertical axis) receiving different proportions of total income (along the horizontal axis). The shape of the curve then indicates how evenly or unevenly income is distributed. If income were equally distributed between households, with 10% receiving 10% of income, 20% receiving 20% and so on, the relationship between the two would then be represented by a straight line at 45 degrees to each axis. The more the distribution varies from this — ie the more unequal it is — the more concave the curve (Graphs 30–41 show the curves for each Member State covered by the ECHP before and after transfers).

For all Member States, a significant proportion of households have little or no income at all without social transfers, reflecting predominantly the large number of people in retirement with no other source of income apart from old-age pensions, though also the relatively large number of unemployed in some cases (Ireland, in particular). The proportion in 1993 varied from 35% in Belgium and over 30% in Ireland, Italy and the UK to under 25% in Greece and Luxembourg.

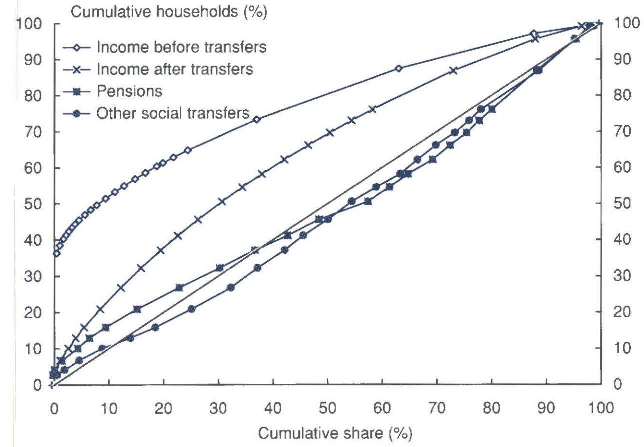
A summary measure of the concavity of the Lorenz curves for each country — ie the evenness, or unevenness, of income distribution — is given by the Gini coefficient (which is calculated as the ratio between the area between the Lorenz curve and the 45 degree line in the graph and the total area above the 45 degree line). The value of this varies between 0, where there is a perfectly equal of distribution of income (ie the Lorenz curve is the 45 degree line), and 1 where there is perfect inequality, with one household receiving all the income. The higher the value of the Gini coefficient, therefore, the more uneven the dispersion of income between households.

In the Union in 1993, for 7 of the 12 Member States, the Gini was much the same before transfers, varying only between 0.54 and 0.56, with the UK having the highest value, and the most uneven income distribution, Spain, France, Ireland and Italy, only a slightly less uneven distribution and Belgium and Portugal, one which was only a little less uneven than for these four. The least uneven distribution of income was in Denmark (with a Gini of 0.48), with that in Germany being only a little more uneven (0.49), while in Greece, Luxembourg and the Netherlands, the degree of dispersion was midway between that in Denmark and that in Belgium or Portugal.

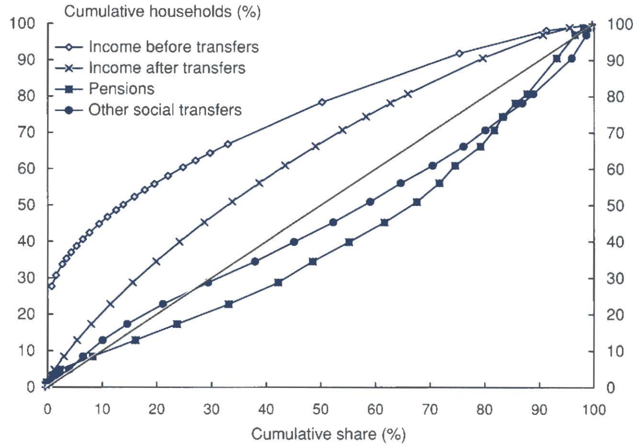
The distribution in each case reflects, it should be recalled, both the initial pre-tax distribution of earnings — returns from financial assets as well as wages and salaries — and the incidence of direct taxes and social charges. In the UK, it would, therefore, appear that either earnings are more dispersed than in other Member States or the direct tax system is less progressive or some combination of the two is at work, while in Denmark, the reverse is the case.

The Gini coefficient, however, summarises only the overall distribution of income and does not necessarily indicate the relative shares going to those at the bottom end of the income scale, which is the main concern here. In other words, a high value of the coefficient might reflect a very uneven distribution of income at the top end of the scale rather than among low income earners. Nevertheless, in practice, the proportion of households in the different Member States with less than 50% of average income before transfers and with less than 65% — the two main groups on which the analysis here is focused —is broadly in line with the differences in Gini values. The proportion is highest in the UK, where just under 43% of households had income below half the average before transfers and 47% less than 65% of average, and only slightly less in Ireland, and lowest in Denmark and Germany (where the figures are 36–37% for under half the average and 41–42% for under 65% of the average), as well as in Luxembourg (Table 5).

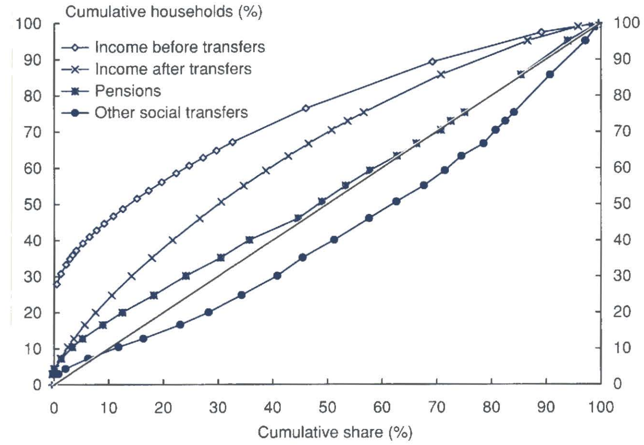
30 Cumulative distribution of net income, pensions and other social transfers in Belgium, 1993



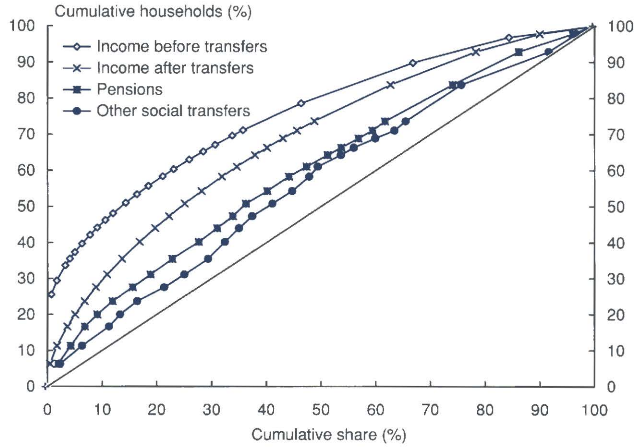
31 Cumulative distribution of net income, pensions and other social transfers in Denmark, 1993



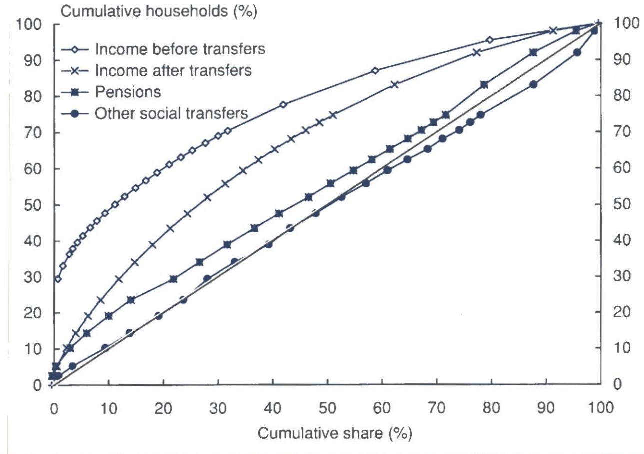
32 Cumulative distribution of net income, pensions and other social transfers in Germany, 1993



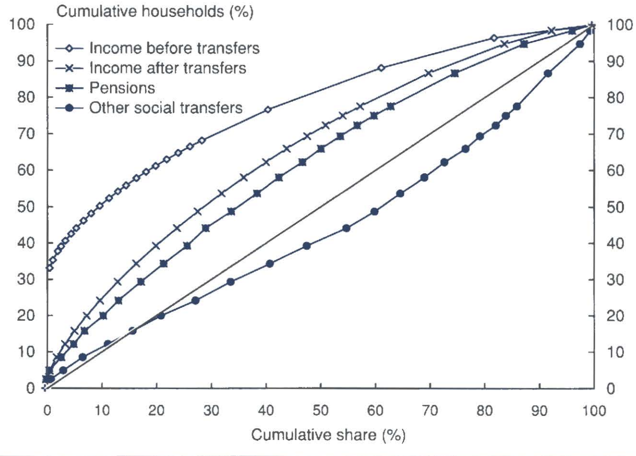
33 Cumulative distribution of net income, pensions and other social transfers in Greece, 1993



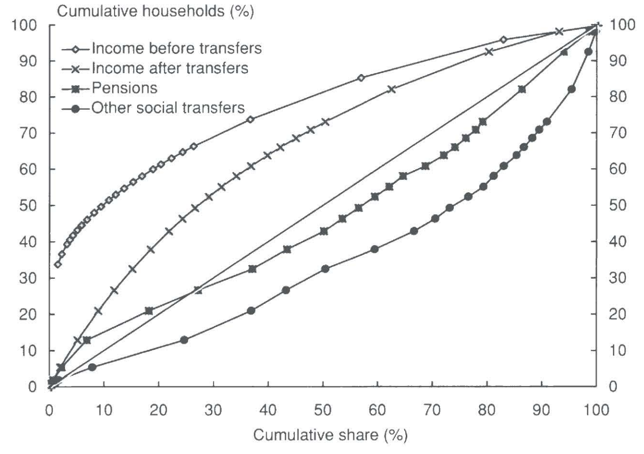
34 Cumulative distribution of net income, pensions and other social transfers in Spain, 1993



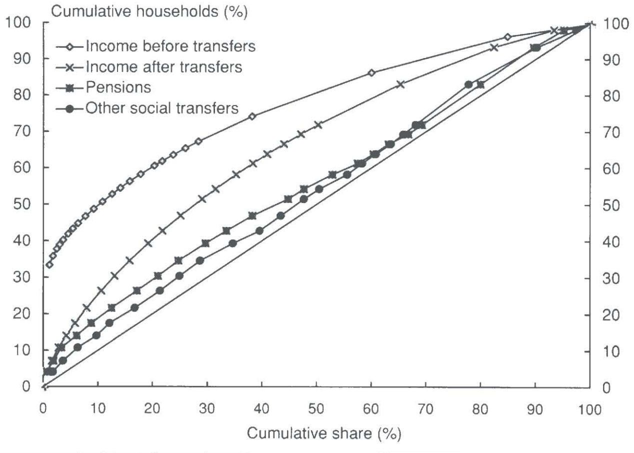
35 Cumulative distribution of net income, pensions and other social transfers in France, 1993



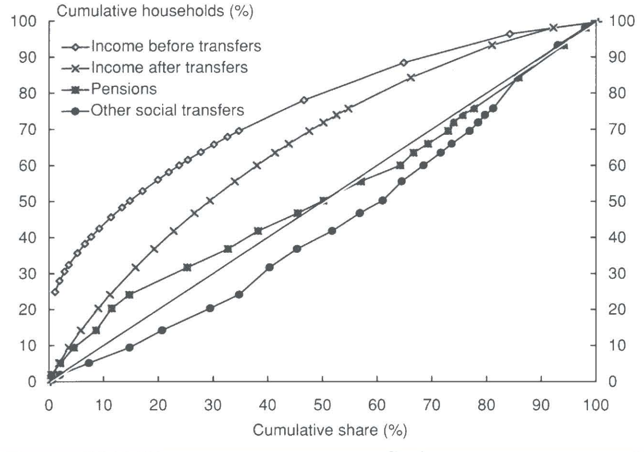
36 Cumulative distribution of net income, pensions and other social transfers in Ireland, 1993



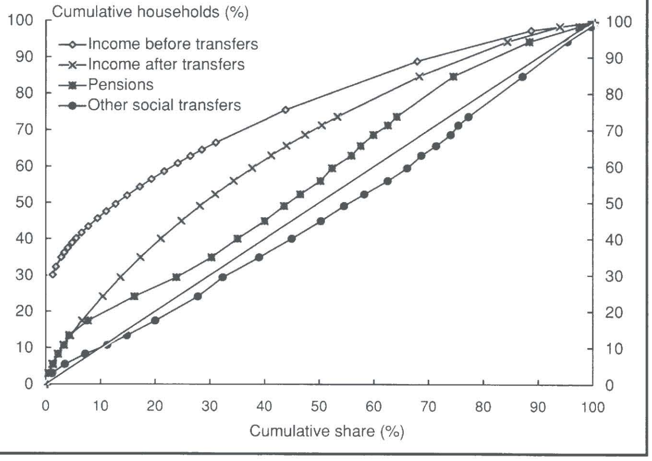
37 Cumulative distribution of net income, pensions and other social transfers in Italy, 1993



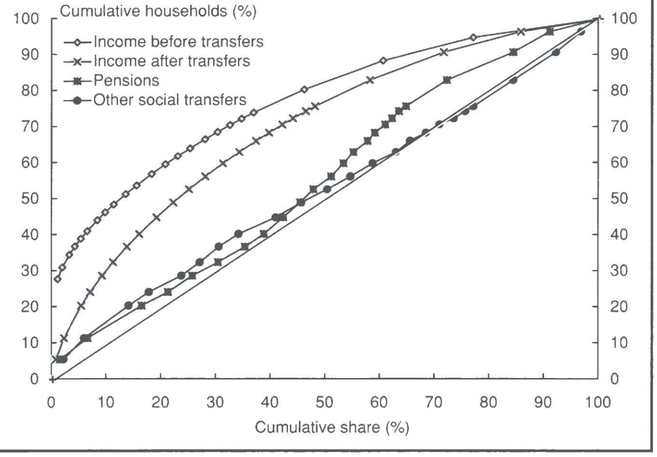
38 Cumulative distribution of net income, pensions and other social transfers in Luxembourg, 1993



39 Cumulative distribution of net income, pensions and other social transfers in the Netherlands, 1993



40 Cumulative distribution of net income, pensions and other social transfers in Portugal, 1993



41 Cumulative distribution of net income, pensions and other social transfers in the UK, 1993

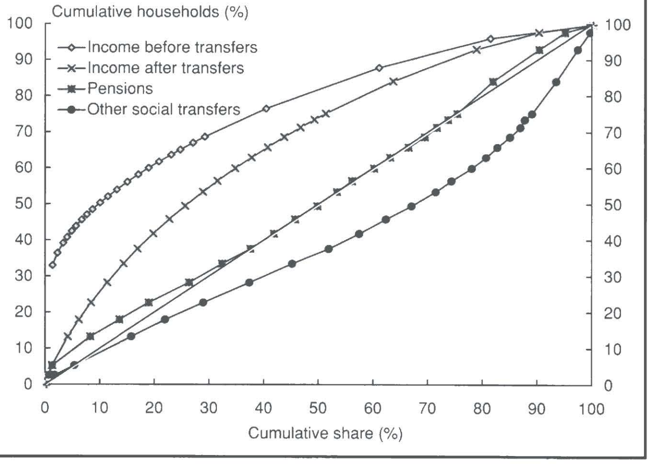


Table 5 — Social transfers and the distribution of household income, 1993

	B	DK	D	GR	E	F	IRL	I	L	NL	P	UK	E12
Transfers as % net household income	36.5	30.5	27.9	24.8	29.7	37.4	27.8	32.7	27.0	30.2	22.1	27.3	30.4
Gini coefficient before transfers	0.544	0.485	0.490	0.511	0.540	0.554	0.553	0.546	0.511	0.512	0.543	0.558	0.532
Gini coefficient after transfers	0.281	0.246	0.286	0.368	0.340	0.312	0.333	0.330	0.318	0.315	0.405	0.357	0.319
Change	0.26	0.24	0.20	0.14	0.20	0.24	0.22	0.22	0.19	0.20	0.14	0.20	0.21
Before transfers													
Households < 50% average income (%)	42.5	37.1	36.0	37.4	39.6	40.6	42.0	40.5	35.9	37.7	39.0	42.6	39.4
Households < 65% average income (%)	45.5	42.5	41.1	44.2	45.6	46.2	46.4	45.0	42.7	41.9	46.3	47.2	44.5
After transfers													
Households < 50% average income (%)	13.0	8.5	12.8	23.7	19.1	15.7	21.2	17.7	14.5	13.6	28.8	22.8	17.1
Households < 65% average income (%)	26.9	22.9	24.8	35.5	34.1	29.3	38.1	30.6	31.9	29.6	40.3	37.7	30.6
Change (% point)													
Households < 50% average income	29.5	28.6	23.2	13.7	20.5	24.9	20.8	22.7	21.5	24.1	10.3	19.8	22.3
Households < 65% average income	18.6	19.6	16.3	8.7	11.5	16.9	8.2	14.4	10.8	12.3	6.0	9.5	13.9

Income distribution after transfers

Social transfers have the effect of reducing the dispersion of income between households markedly in all countries, which, of course, is only to be expected, the largest reduction occurring at the bottom end of the income scale for households which have little or no other source of income but the social protection system. They also, however, have the effect of widening the difference in income disparities between Member States, partly because of the differing scale of transfers noted above, partly because of differences in the way they are distributed between income groups.

After transfers, income remained more evenly distributed in Denmark in 1993 than in any other Member State (the Gini coefficient being 0.25), with the distribution in Germany (0.29) also being more even than in most other countries, though slightly below that in Belgium (0.28), which had the second most even distribution. At the other end of the scale, income was least evenly distributed in Portugal (where the Gini was 0.41), with Greece having the next most uneven distribution (0.37), followed by the UK (0.36). In between, the distribution in Spain, Ireland and Italy was similar in each case and slightly more uneven than average (with the Gini being around 0.33–0.34), and in France, Luxembourg and the Netherlands, a little less uneven than average (0.31–0.32).

The narrowing of disparities achieved by social transfers was, therefore, greatest in Belgium, which had a wider than average dispersion of income before transfers and the second narrowest after, followed by France, where the dispersion was also wider than average before transfers but narrower afterwards. In both cases, the effect of transfers on income distribution reflects the scale of these, which was larger than in other Member States (Graph 42). At the same time, the reduction in income disparities in Denmark was similar to that in France, but the relative scale of transfers was much less. Similarly, the reduction in Ireland was much the same as in Italy, but the amount transferred was significantly greater in the latter than the former, implying that transfers were more effective in narrowing income disparities in Ireland than in Italy. Much the same is true of Germany and the UK, on the one hand, and Spain and the Netherlands, on the other, a similar reduction in disparities resulting from larger transfers in the latter two countries than in the former two.

The effect of social transfers on income distribution was least evident in Greece and Portugal, where the amount transferred was less than in the rest of the Union, though in Greece, the scale of transfers was greater than in

Portugal, implying that they were less effective in these terms.

The effect of transfers on low income households

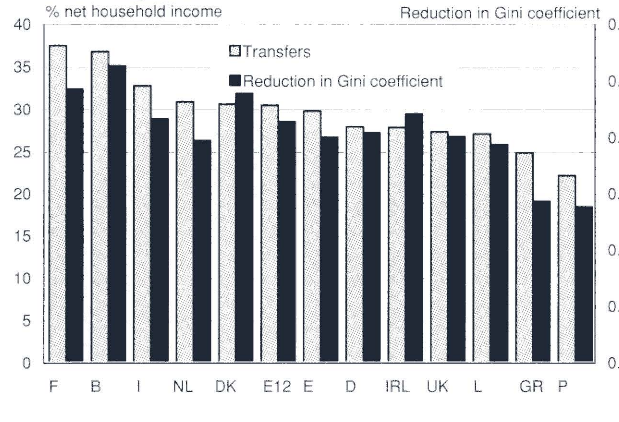
Nevertheless, as noted above, changes in the value of Gini coefficients are summary measures of changes in the overall distribution of income and do not necessarily indicate what is happening at the lower end of the distribution which is of greatest relevance in the present context. In practice, there are some differences in the effect of social transfers on households with the lowest levels of income from that implied by changes in the Ginis. In particular, the reduction in the proportion of households with less than half average income and with less than 65% of the average was greater in Denmark (by 28½ percentage points in the former case) than in France (25 percentage points), even though the reduction in the Gini was much the same, while, similarly in Germany and the Netherlands, the reduction (of 23 and 24 percentage points, respectively) was greater than in the UK or Spain (20 percentage points), where again the Gini was reduced by the same amount (Graph 43). In addition, in Greece, where the reduction in the Gini was the same as in Portugal, the proportion of households with income of under half the average was reduced by more than in the latter (13½ percentage points as against 10½).

These comparisons reflect in some degree the extent to which social transfers were concentrated on low income households. They also reflect, however, the underlying, pre-transfer, distribution of income, which was more even in Denmark than France (or anywhere else), in Germany and the Netherlands than in the UK or Spain and in Greece than in Portugal. The amount of transfers required to bring households with below 50% of average income up to this level was, therefore, less in the former countries in each pairing than in the latter.

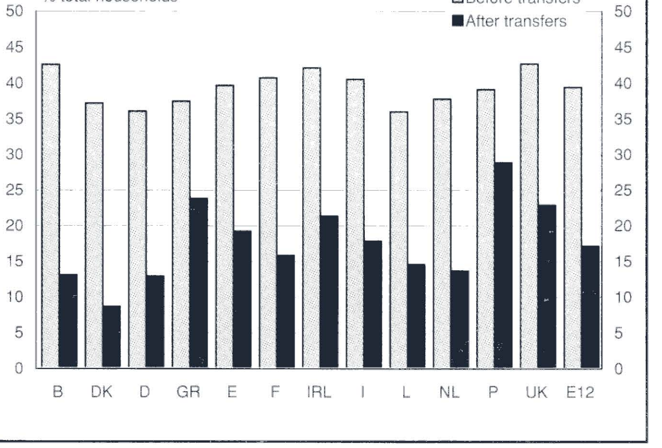
Even after social transfers, a significant proportion of households in most countries remain with income of less than 50% of the national average, which is the measure of the poverty level of income conventionally used (and which, moreover, was agreed as a working definition by the Council of Ministers in December 1984). This proportion, as indicated above, is greatest in Portugal, where around 29% of households had a poverty level of income in 1993 according to this measure, and second highest in Greece, where the figure was just under 24%. The proportion was only slightly lower in the UK (23%), though given the much higher level of average income here than in either of the other two countries, the absolute level of income received even by households below the poverty line so defined was markedly higher.

Since the countries with the next highest proportions are Ireland and Spain (21% and 19%, respectively), which are also countries with income per head — or per household — below the Union average, there is some association between low income and the relative number of households with income below the poverty level. Similarly, in high income Member States, a

42 Social transfers as a share of household income and reduction in income inequality in Member States, 1993



43 Households with less than half average net income, before and after social transfers in Member States, 1993



relatively low proportion of households tend to have poverty-levels of income — only 8½% in Denmark and 13% in Belgium and Germany. The association, however, is not systematic, in the sense that Luxembourg, the country with the highest income per head in the Union by some way, has proportionately more households with income below the poverty line than in these three countries, while, as noted above, the UK, has a higher proportion than either Spain or Ireland.

To some extent, this relationship reflects the greater ability of the more prosperous Member States to finance social transfers and, accordingly, to provide assistance to households with little or no income from employment or financial assets, the relative number of which, as indicated above, was much the same in most Member States. At the same time, as also indicated above, there is by no means a perfect association between the scale of transfers and the amount of these that are distributed to the lowest income households or, as shown below, the allocation of the amount which is transferred between the households concerned.

The scale of poverty

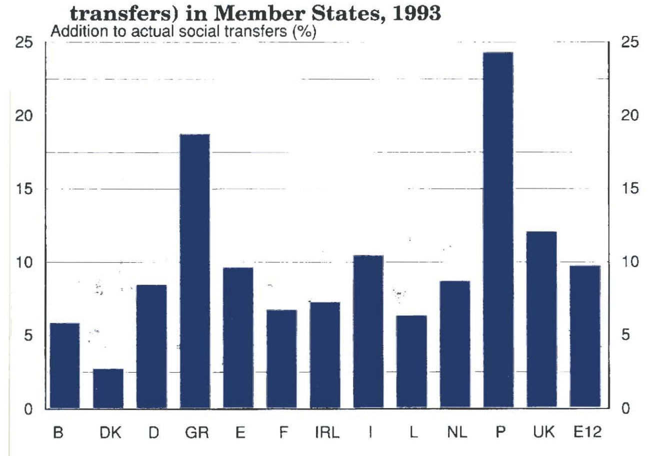
The relative number of households with below 50% of average income is only a partial indicator of the scale of the poverty problem in different Member States, defining poverty in this sense. The extent to which households fall below this level is also of relevance. If, for example, households below the poverty line had an income level only slightly below half the national average this would lead to a different assessment of the scale of the problem — and the effectiveness of social protection systems — than if it were substantially below.

One way of measuring this is to estimate the amount of additional transfers that would be necessary in each country to bring all households below half average income up to this level, assuming, of course, that it were appropriately allocated between them (not an easy matter in reality given the difficulty of identifying such households and the lack of information about their income). This also, of course, gives an indication of how much extra expenditure on social protection would be required to eradicate this particular problem, given the (relatively narrow) way it is being defined.

The calculation shows that over the Union as a whole, an increase in social transfers of just under 10% in 1993 would have been sufficient to bring the income of all households up to at least half the average in the countries where they are located, assuming this additional sum was transferred from those well above the poverty line to avoid them sinking below it when the counterpart taxes or contributions are levied. (Alternatively, an equivalent amount of transfer could have been diverted from those well above the poverty line, who received a significant proportion of the total as indicated below, without any overall increase in total transfers.) In Denmark, it could have been achieved with a rise of under 3% in transfers and in Belgium and Luxembourg, one of around 6% (Graph 44). On the other hand, in Portugal, transfers would have needed to increase by almost 25% and in Greece, by around 19%, significantly more than in the UK (12%), despite the share of households with below half average income being only slightly higher.

Indeed, there are some revealing differences between the extra transfers required and the share of households with income less than half the national average. In Ireland, for example, where this share was above that in most other countries, the additional transfers amount to around 7%, lower than in most countries, including Germany and the Netherlands (around 8½% in both cases), where the share was much less. This implies that the extent to which households fell below the poverty line was, on average, much less in

44 **Increase in social transfers needed to raise all households above the poverty line (after transfers) in Member States, 1993**



Ireland than in these two countries — as, indeed, in the UK as compared with Greece. To a smaller extent, the same is true of France, where the required rise in transfers is only around $6^1/_2$%, again less than in Germany or the Netherlands, where the share of households with below half average income was lower.

The distribution of transfers between households

In practice, households with income below half the average level before transfers receive most of the amount that is transferred in all Member States. Over the Union as a whole, over three-quarters of social transfers went to such households in 1993. However, whereas the proportion was around 75% in most countries — and almost as high as 80% in France — it was significantly below this in Portugal (69%) and Greece (70%), the countries with the lowest overall scale of transfers in the Union. The relatively large number of households in these Member States with income below half the average *after* transfers, therefore, reflects not only the smaller amount of income which is transferred than elsewhere but also the smaller share which goes to the poorest households.

The counterpart of this is the relatively large share of transfers in these two countries going to households with income above average before transfers. In 1993, 16% of the total went to such households, a higher proportion than anywhere else in the Union, and given that under 40% of households are included in this income group, the average amount received was significant. The proportion of transfers going to households in this group was the same in Belgium, though their relative number was higher, and only marginally lower in Spain and Italy. By contrast, only 9% of transfers went to households with above average income in Germany and France (though the average amount received was much more in the latter than the former) and only 10% in Denmark and the Netherlands.

Most of the households on which transfers are concentrated had little or no other source of income. Indeed, over 60% of transfers in most countries went to households with income of under 20% of the average before transfers in 1993. The figure for pensions alone was even higher at over 70% in the majority of countries, implying that most pensioner households were solely reliant on the income received from these. Over the Union as a whole, over 80% of pensions went to households with income of less than half the average before transfers, and in Germany and France, over 85%. The proportion was less than elsewhere in the four Southern Member States, at around 75%, reflecting the greater prevalence of the extended family, though it was also around this level in the UK, where income from capital was relatively important.

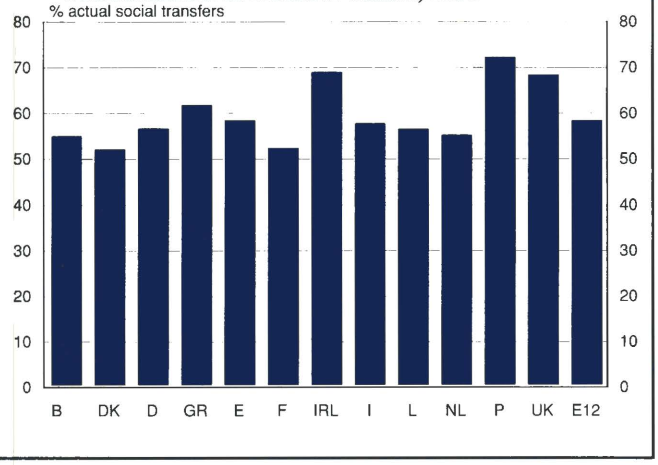
As might be expected, transfers other than pensions are less concentrated on the poorest households, partly because in many cases they are intended to provide replacement income for a temporary period, partly because they include family or child benefits payable to everyone. Just over half of unemployment benefits in 1993 were paid to households with income of less than 50% of average before transfers, the proportion being as high as 75% in Ireland and Luxembourg. The proportion, however, was less than half in all four Southern Member States, and only around 40% in Italy and as low as 22% in Greece, reflecting in part the fact that more of the unemployed live in households with other people in work than in Northern Member States, as noted in Chapter 1, in part the relative concentration of benefits on the better paid members of the work force.

Other benefits, including those for sickness, disability and children, were more concentrated on the poorest households, just over 60% of the total amount transferred in the Union going to households with income below half the average. For these transfers, the concentration on such households was greatest in Denmark and the UK, their share being just under 75% in both cases (in the UK, partly because of the inclusion of income support to the unemployed, especially long-term unemployed, in these), while again it was relatively low in Greece and Portugal, the share being only around 50%. This, however, was more than in Belgium or Luxembourg, where households with under half average income received under 45% of the total transferred.

This, however, is only part of the picture. While most transfers go to the lowest income households, they are by no means evenly distributed between them in any of the countries. If they were, then poverty as defined here would be eliminated. This can be illustrated by the simple exercise of adding the average transfer per household going to those below the poverty line before transfers (ie the total amount transferred divided by the number of households with income from other sources of less than half the average) to the average income from other sources. The result is a level of income well above the poverty line (after transfers) in all Member States, including Greece and Portugal.

A further exercise, which is instructive, is to calculate the total amount of transfers which would be required to lift the income of all households from below the poverty line — defined after transfers — to the line itself (ie to transfer just enough to each household with income of less than half the average to bring its income up precisely to this level, which by definition would eliminate poverty). In the Union as a whole, this aim could be achieved with 58% of the total amount actually transferred in 1993, the proportion varying from around 50% in Denmark (where pre-transfer income is more evenly distributed than elsewhere) and France (where the scale of total transfers is large) and around 55% in Northern mainland Member States to just over 70% in Portugal (where transfers are relatively small) and just under 70% in Ireland and the UK (where income before transfers is relatively unevenly distributed and where, therefore, for many households, the income from other sources falls substantially below the poverty line) (Graph 45).

45 Social transfers needed to raise all households above the poverty line if appropriately redistributed in Member States, 1993



The clear implication is that the transfers going to households with the lowest levels of income from other sources are relatively unevenly distributed between them, with some receiving inadequate amounts to bring their total income up to the poverty line and others receiving much more than this, so having their income raised to well above the line and, in a number of cases, to well above the average. As indicated below, this is predominantly explained by the uneven distribution of old-age pensions, which account for the major part of transfers.

Transfers by income group

Whereas the distribution of transfers other than pensions tends to be slanted towards low income households, measuring income here after rather than before transfers, this is not the case for pensions in many Member States. In other words, though most of households who received pensions had little or no income coming from other sources, for a significant proportion, the amount received resulted in their net income being increased considerably in relation to that of households in general.

Indeed, the only Member States where pensions went disproportionately to households with below average income after transfers rather than above were Belgium, Ireland and, most especially, Denmark. In three other Member States — Germany, the UK and Luxembourg — the distribution of pensions between income groups was broadly proportionate, while in the other six (the four Southern Member States plus France and the Netherlands), households in the upper income groups received a disproportionate amount of the total transferred in the form of old-age pensions. (The distribution of pensions as well as other transfers between households ranked according to post-transfer income is shown in Graphs 30–41 above; in these cases, the more convex the curve, the greater the amount going to lower income households.)

In terms of the households with the lowest income levels, in none of the Member States did households with under half average income after transfers receive a disproportionate share of old-age pensions and only in Denmark was their share proportionate. In France, for example, the 16% of households with income of this level received only 7% of total pensions and in Italy, the 18% of households in question received only 8% of total pensions (Table 6).

By contrast, the 13% of households with income of $1^1/_2$ times the average or more in France received 25% of total pensions, in Portugal, the 17% of households in this category re-

Table 6 — Distribution of transfers, households and income by broad income group, 1993

		B	DK	D	GR	E	F	IRL	I	L	NL	P	UK	E12
Income after transfers relative to national average														*% total*
< 50%	Pensions	7	9	6	12	10	7	18	8	8	4	25	19	9
	Unemployment benefits	18	3	16	12	21	14	42	15	21	12	10	32	17
	Other social	12	4	15	18	19	16	34	11	21	9	29	29	19
	Household numbers	13	9	13	24	19	16	21	18	14	14	29	23	17
	Total income	4	3	4	7	7	5	9	5	6	4	9	8	6
50–65%	Pensions	16	25	13	11	17	10	25	12	17	20	13	19	14
	Unemployment benefits	27	15	19	9	14	16	23	10	36	19	10	15	17
	Other social	14	13	16	14	14	19	22	14	19	16	10	24	19
	Household numbers	14	14	12	12	15	14	17	13	17	16	12	15	13
	Total income	8	8	7	7	9	8	10	7	10	9	7	9	8
65–100%	Pensions	42	41	40	25	32	30	25	32	41	28	19	26	33
	Unemployment benefits	31	48	38	22	33	37	23	27	18	28	36	29	35
	Other social	31	55	38	20	30	40	24	33	33	39	30	28	35
	Household numbers	31	38	34	26	28	33	23	28	32	30	26	25	30
	Total income	26	32	28	21	23	27	18	22	25	24	21	21	25
100–150%	Pensions	23	19	28	27	21	28	18	27	19	22	15	19	25
	Unemployment benefits	18	30	20	33	22	21	9	20	19	25	24	17	21
	Other social	29	25	20	25	24	18	14	23	14	22	17	12	18
	Household numbers	29	30	26	23	21	25	21	25	21	25	17	21	24
	Total income	35	36	32	28	25	30	26	30	25	31	21	26	30
> 150%	Pensions	11	6	14	26	21	25	14	20	15	26	28	18	19
	Unemployment benefits	5	5	7	24	11	12	3	29	5	16	20	7	10
	Other social	14	3	11	23	13	7	6	19	13	14	14	6	9
	Household numbers	13	9	14	16	17	13	18	17	15	15	17	16	15
	Total income	27	20	29	37	37	30	38	35	34	32	42	37	32

ceived 28% and in Greece and the Netherlands, the 15–16% received 26% of the total, implying that in these countries, pensions were relatively unevenly distributed between households — indeed, in France and the Netherlands, not much less so than total income.

Social transfers other than pensions were, as might be expected, slanted more towards lower income households. Nevertheless, in Greece, Portugal and Italy, these too were disproportionately paid to households with above average income rather than to those with income below the average, though it should be borne in mind that the scale of such transfers was much less than in other countries and the coverage narrower. For example, in all three cases, even unemployment benefits went more to the richer households than the poorer ones, 29% of the amount paid in Italy, for example, going to the 17% of households with income of 1½ times the average or more and in Portugal, only 10% going to the 29% of households with income of under half the average, again partly reflecting the relatively high proportion of the unemployed living in households with people in work.

By contrast, in Ireland, where unemployment benefits are flat-rate and relatively low, 42% of the total transferred went to the 21% of households with income of under half the average and in the UK, which has a similar system, 32% went to the 23% of households in this category. On the other hand, in the other Member States, though households with below average income received a disproportionate share of unemployment benefits and other social transfers, this was not so in all cases

Table 7 — Characteristics of households with low income and share of household types with low income, 1993

	B	DK	D	GR	E	F	IRL	I	L	NL	P	UK	E12
Composition of households (% total)													
Pensioner	23	25	22	21	17	22	17	22	18	21	18	24	22
Couples with children	21	15	19	22	25	22	27	18	20	19	26	19	20
Lone parents	3	3	3	1	1	3	3	1	1	2	2	4	3
Childless households	30	46	39	21	14	32	18	20	34	42	14	31	30
Other	23	10	17	35	44	21	35	38	27	16	41	21	25
Total	100	100	100	100	100	100	100	100	100	100	100	100	100
Composition of households with income < 50% average (%)													
Pensioner	29	42	29	39	18	29	25	24	26	25	34	38	30
Couples with children	18	6	13	14	26	14	28	18	26	14	19	19	17
Lone parents	6	3	7	1	1	5	11	1	3	5	1	10	5
Childless households	27	45	38	17	11	35	19	14	23	38	13	20	25
Other	20	3	13	29	44	17	18	43	22	17	33	13	23
Total	100	100	100	100	100	100	100	100	100	100	100	100	100
Households with income < 50% average (% household type)													
Pensioner	17	15	18	44	21	21	32	18	21	16	55	36	24
Couples with children	11	4	9	16	20	10	22	17	18	10	21	22	14
Lone parents	23	8	34	27	30	24	65	24	32	38	27	53	36
Childless households	12	8	12	19	16	18	22	12	10	12	28	15	14
Other	12	2	10	19	19	13	11	20	12	14	23	14	16
All households	13	9	13	24	19	16	21	18	14	14	29	23	17
Households with income < 65% average (% household type)													
Pensioner	41	44	36	61	49	37	67	41	45	47	71	62	46
Couples with children	19	10	19	26	33	22	35	29	36	28	30	33	26
Lone parents	50	29	51	33	35	40	78	33	32	73	60	76	55
Childless households	23	18	21	29	26	29	30	18	26	21	39	25	23
Other	22	12	22	31	31	28	28	31	27	26	33	26	28
All households	27	23	25	36	34	29	38	31	32	30	40	38	31

of households with the lowest levels of income. Indeed, in Denmark, the 23% of households with income of less than 65% of the average received only 18% of unemployment benefits and 17% of other transfers, which in this case, reflects the relatively generous level of payment, while in the Netherlands, they received a proportionate amount.

Who are the poor?

The final step in the analysis is to examine the characteristics of households with low income, especially those with levels below the poverty line even after transfers, since these represent the households which merit the closest consideration in any reform of the social protection system. They are also the ones which existing social welfare arrangements have, in some sense, failed to assist sufficiently to lift their income above the poverty level, though it should be emphasised that social policy in the Member States concerned is not specifically aimed at achieving this objective defined in this particular way. In other words, while the relief of poverty is a major aim in all countries, the precise interpretation of this differs from country to country.

For purposes of analysis, households can be divided into five groups:

- pensioner households, or those with a single person or a couple of 65 or over, which accounted for some 22% of total households in the Union in 1993, the proportion ranging from 25% in Denmark and 24% in the UK to 18% in Portugal and 17% in Spain and Ireland;
- lone parents, or households with someone of 16 or over living with a child or children under 16, which accounted for just $2^1/_2$% of total households in the

Union, though 4% in the UK and 1% in Greece, Spain, Italy and Luxembourg;

- couples under 65 with children, which represented 20% of total households in the Union, but 27% in Ireland, 26% in Portugal and 25% in Spain, though only 15% in Denmark and 18% in Italy;

- couples or people living alone without children, which accounted for 30% of households in the Union, but 46% in Denmark and 42% in the Netherlands, though only 14% in Spain and Portugal and 18% in Ireland;

- other households, which are those whose members are both over 65 and under 65, those with more than two people of 16 or over and so on (ie in many cases, extended households), which represented 25% of the total in the Union, but 44% in Spain, 41% in Portugal and 38% in Italy and only 10% in Denmark, 16% in the Netherlands and 17% in Germany.

Pensioner households, as defined above, accounted for 30% of all households with income of under half the average in the Union in 1993, proportionately more than their share of the total (22%). In Denmark, however, 42% of households with this level of income consisted of people of 65 or over (though since very few households overall had income this low, the relative number involved was also low, as indicated below), in Greece, 39% and in the UK, 38% (Table 7). On the other hand, in Spain, pensioner households represented only 18% of those in this income group, which, nevertheless, was slightly higher than their share of all households. Moreover, Spain was the only country where the proportion was less than 24%, and in all Member States, the figure was higher than the overall proportion of pensioner households. In general, therefore, pensioner households were more likely to have a poverty level of income than other types.

Lone parents with at least one child under 16 were also in most countries much more likely than other households to have income below the poverty line. In the Union as a whole, they accounted for 5$^1/_2$% of all households in this category in 1993, though for 11% in Ireland and 10% in the UK and only 1% in all four Southern Member States.

Each of the three other types household were, in general, less likely than these two kinds to have income of under half the average — the main exception being couples with children in Luxembourg — though in all Member States, they represented the largest *number* of households with poverty levels of income.

Low income by household type

The chances of a particular household type having income below the poverty line can be inferred from the above figures. They can, however, be calculated more directly. Such a calculation shows that some 36% of lone parents in the Union with a child under 16 had a level of income which was under half the average in 1993, and 55% income of below 65% of average. Almost all of the people concerned were women (as indicated in Chapter 1). In Ireland, the proportion of lone parents with a poverty level of income was as high as 65% and in the UK, 53%, while in both countries, over three-quarters of lone parents had income under 65% of average. These figures are by some way higher than in the rest of the Union — the Netherlands apart, where 73% of lone parents had an income of under 65% of average — and contrast markedly with the position in Denmark, where only 8% of lone parents households had income of under half the average. Moreover, in Spain, Italy and Luxembourg, lone parents were hardly any more likely to have income of under 65% of the average than other households. Nevertheless, except for these three countries, in all Member States, people living alone with a child under 16 were significantly more likely to have a low income level than households in general.

For pensioner households, there is an equally marked variation between countries. In the Union as a whole, 24% of households consisting of a single person or a couple of 65 or over had an income level below half the average and 46% — ie almost half — one of under 65% of average. In Portugal, however, over half (55%) of pensioner households had income of under half the average and 71% one of under 65% of average, while in Greece, 44% fell into the former category and 61% into the latter, less than in Ireland (67%) and the UK (62%). In these four countries, therefore, retirement from paid employment tends to lead to low levels of income for most households.

In the rest of the Union, the figures are much lower, with only around 20% or less of pensioner households having income below half the average in each case and under half having income of 65% or less. (It should be noted that although 42% of households with half average income in Denmark were pensioner ones, only 15% of pensioner households had an income this low.) However, as in the case of lone parents, these proportions are, in all countries, higher than for other types of household.

Chapter 4 Making unemployment benefit systems more employment-friendly

Systems of unemployment benefit have become an increasingly important focus of policy concern throughout the Union as the number out of work and receiving income support has risen. Although the expenditure to which they give rise is, in all Member States, a relatively small proportion of total spending on social protection, as noted in the previous chapter, the tendency for it to increase during periods of increasing unemployment when budget deficits are also usually widening because of depressed levels of tax revenue gives it added significance. Moreover, the growth of expenditure has been accompanied by growing concern about the potential effect of benefit levels on incentives to look for work and, related to this, about the persistently large numbers of long-term unemployed among those being supported.

In most Member States, changes have been made to benefit systems in recent years with the twin aims of curbing expenditure and of reducing the numbers dependent on income support. This approach has been endorsed by the Commission in its recent Communication, *Modernising and improving social protection in the European Union* as well as by Member States at the Luxembourg Job Summit, both of which advocated a more employment-friendly stance by shifting from passive measures to more active policies designed to increase the employability of those out of work and to help them find jobs.

The concern of this chapter is to examine specific policy developments in Member States in the light of this Communication, the guidelines contained in it and the European Council conclusions at Luxembourg. In particular, it considers the extent to which there has been to move towards an 'activation' of policy and the relative emphasis placed on measures to limit entitlement to benefit and the amount received as opposed to more positive action to help the unemployed into work and increase their chances of finding a job. It begins, however, by examining the philosophy underlying the shift in policy stance towards according more weight to incentive effects and the justification for this in terms of the actual level of unemployment benefits relative to earnings from work.

Shifts in policy emphasis

Since they were first introduced, at the end of the 19th century, unemployment benefits have had two main aims: providing replacement income for workers losing their jobs and helping to regulate the functioning of the labour market. As the number out of work has risen, the increasing cost of providing support has put growing pressure on sources of finance, whether these consist mainly of social contributions or general taxation. It has also prompted, along with the rise in dependency and concern about the social exclusion of those affected, a growing interest in a reorientation of policy effort away from passive towards active measures. Indeed, from both an economic and a social perspective, it is undeniably more efficient to devote resources to getting the unemployed back to work rather than simply supporting their income.

Although the principle is indisputable, the policy can be interpreted and put into effect in very different ways. On the one hand, it can be achieved through reducing unemployment compensation, or tightening the conditions for entitlement to support, so encouraging, or 'activating', the unemployed to intensify their efforts to find a job. On the other hand, it can be conceived of as strengthening the assistance given to the unemployed to get back into work, through such measures as the provision of training, or re-training, counselling, career guidance and help with job search, which can be combined with adequate levels of income support to enable the unemployed to spend time finding a job best suited to their skills and qualifications.

These are not mutually contradictory approaches. Indeed, in many Member States, the two have been pursued in parallel, income support being made less generous, especially as the period spent out of work lengthens, with the aim of accelerating job search, at the same time as more effort has been put into active measures to help the unemployed find a job. The relative weight attached to the two has, however, varied between countries and has been very much influenced by prevailing economic conditions and budget constraints on expenditure growth. This has tended to increase the attraction of the first approach, since it serves to curb expenditure at the same time as it increases incentives to look for work, while the second involves adding to expenditure rather than subtracting from it, unless there is a parallel restructuring of spending, at least until the measures concerned begin to reduce the number of benefit claimants.

The activation of policy has extended beyond the unemployment compensation system alone to encompass other areas of social protection, disability benefits, early retirement pensions and minimum income guarantee schemes, in particular, partly because these are, in effect, alternative ways of providing income support. Indeed, the significant growth in the past in the numbers being supported by these means has been partly due to their politically attractive effect of reducing the number registered as unemployed. More fundamentally, however, they serve to take the people concerned off the labour market, so relieving competition for scarce jobs and making it easier for others, younger people in particular, to find work. It is as much the expansion of recipients of these kinds of benefit as unemployment compensation which has increased the number dependent on social welfare in Member States and prompted a reassessment of policy. This has been reinforced by the growing recognition of the problems of social exclusion suffered by such people.

Moreover, there are signs of increasing concern about the complexity of systems of social protection in relation to those out of work which has resulted from the often piecemeal changes made in response to rising unemployment and labour market imbalances. Compensation systems in most countries now consist of a combination of:

- insurance-based benefits, which are payable for a fixed period of time according to the employment record and age of the person concerned;
- social assistance, which is usually means-tested and comes into effect if there is no entitlement to insurance benefits or if this has elapsed;
- the other income support schemes listed above, which may or may not be means-tested;
- benefits in kind, such as assistance with housing costs which may be linked to the receipt of income support.

The general effect is a lack of transparency for beneficiaries, and accordingly a high degree of uncertainty about the consequences of any changes in their circumstances, which is liable to discourage them from trying to improve their position and from actively looking for a job, quite apart from any disincentives created by the level of benefits in relation to potential earnings from work. An additional effect is that it makes it difficult to describe the systems in operation in Member States and to assess the relative amounts received by those being supported.

The generosity of unemployment benefits

The general re-assessment of levels of unemployment compensation which has occurred across the Union reflects a combination of concerns. Not only is it aimed at curbing expenditure, but, as noted above, it is designed to increase the financial pressure on the unemployed to find a job. It is also a response to changing attitudes towards redistributive policies in economies where real income growth has been depressed for some time and where a growing reluctance to accept large-scale social transfers and the high tax regimes which they imply is evident in many Member States (in changing political philosophies, in particular). While popular support for systems of social protection remains strong, it is clear that such support is conditional on both the level of benefits being perceived as fair and reasonable in relation to the income earned by those in work and on entitlement to benefit being properly controlled.

At the same time, Governments have to strike a balance between curbing expenditure and increasing the financial pressure on the unemployed to look for work, on the one hand, and providing acceptable levels of income support, on the other. In this regard, it is apparent that the balance has shifted, in part because interpretations of the level of transfer which is considered as acceptable have changed. Moreover, whereas previously there was some emphasis on the need for income support to be high enough to give the unemployed sufficient time to find a suitable job, which was regarded as not only in their interests but also in the interests of improving the functioning of the labour market and increasing macroeconomic efficiency, the main aim now is to accelerate job search activity and get people back into work as soon as possible. This reflects not just a concern to keep expenditure down but also a recognition of the change in economic circumstances, of the reduction in jobs on offer and of the possible need for the unemployed to seek a different kind of job than the one held before, combined with the evidence that the chances of finding work diminish as the spell of unemployment lengthens.

In practice, the conflicting objectives in this regard, of providing acceptable levels of compensation while encouraging job search activity and curbing expenditure, have been reconciled in a number of Member States by tightening the criteria for eligibility for unemployment benefit and broadening the definition of what is deemed to be a suitable job. In particular, recipients have to demonstrate that they are both actively seeking work and, after a time, are willing to accept any reasonable offer of employment if they are capable of doing the job, irrespective of how it compares to what they were doing before.

This kind of solution makes it difficult to evaluate the incentives to find a job implied by unemployment compensation systems in different countries or how they have changed over time — or, from the opposite perspective, the incentive to remain out of work or deliberately to become unemployed — since their strength will depend not only on the level of benefits payable in relation to potential earnings from work but also on the conditions imposed on receiving benefit. Moreover, the difficulty is further complicated by the fact that what matters in the latter regard is not the statutory instruments in force, which can readily be examined and compared between countries, but the way these are interpreted and enforced, which is much more difficult to assess.

Accordingly, it is equally hard to predict the effect on unemployment, or on the number of people receiving income support, of the changes to systems which have been made in recent years and which are now in the process of being implemented. Although they might be expected to reduce the average duration of unemployment as people take up jobs more quickly than they otherwise might do, if there is no increase in the jobs on offer, the fall in the numbers unemployed is likely to be limited (to the number of vacant jobs which people are persuaded to take up). While there might be a faster turnover of the unemployed, any reduction in the generosity of benefits could make people in work more reluctant to change their job because of the risk of becoming unemployed and more prepared to remain in a job they are not suited for, so increasing job mismatches and reducing economic efficiency.

The question of the effect on unemployment of the benefit systems in operation is one which has exercised economists for some time, particularly as the number of people out of work has risen. Though much research effort has been devoted to assessing the nature and scale of the effect, no satisfactory estimates have been produced, largely because of the difficulties noted above. Indeed, these difficulties have led to the conclusion that it is much too simplistic to consider benefit levels alone and that it is essential to consider the compensation system as a whole, including the various controls and restrictions which operate. The widespread view across the Union is that while benefit systems may, in a number of countries, have contributed to the high rates of unemployment which now prevail and, in particular, to the substantial numbers of long-term unemployed, they cannot plausibly be regarded as the main factor underlying either. Accordingly, the measures now being taken to modify their operation might help to reduce both, but they cannot be expected to represent the major part of the solution to the problem.

Benefit levels relative to earnings

In practice, it is difficult to estimate levels of benefit in meaningful terms across the Union, ie in relation to the

The ECHP data used in the analysis

Data from the ECHP give an insight into the wages which those experiencing a spell of unemployment were earning when employed or were paid when they returned to work. Specifically, the data relate to the average monthly earnings from employment of those who were unemployed for at least three months during 1993, and drawing benefits, and in a full-time job for at least one month. Although they do not enable earnings received before becoming unemployed to be distinguished from those received from a job obtained after a person was unemployed, they, nevertheless, provide an indication of the wage which the men and women concerned can command. (In this sense, they are different from 'replacement rates' as nomally defined, which relate to benefits in relation to previous earnings from work.)

The benefits included in the analysis are those linked to unemployment and cover social assistance as well as social insurance benefits. They exclude, however, transfers which are paid specifically to households, such as to cover housing costs. They are measured net of any direct taxes or social contributions payable on them, except in France, where they include direct taxes not deducted at source. The average monthly amounts are calculated as the sum of benefits received during 1993 divided by the number of months of unemployment. Earnings from employment are also net of direct taxes and social contributions, except in France where they are gross of taxes not deducted at source, and are calculated in a similar way by taking the sum of earnings during 1993 and dividing by the number of months of employment. Those employed part-time are excluded from the analysis.

earnings which someone unemployed could obtain if they were working, let alone to assess the effect of the various kinds of restrictions on eligibility. Up to now, the only feasible means of making estimates has been to construct models of replacement rates — benefits relative to disposable income when in work — containing details of the unemployment compensation system, on the one hand, and of the tax system, on the other, and feeding into these assumptions about the earnings and the personal characteristics of the person unemployed (age, marital status and so on). The new European Community Household Panel (ECHP), however, gives for the first time an insight into the amounts actually received by those who are unemployed in the different Member States. Eventually, as the annual surveys of the panel (or 'waves') are carried out, it ought to be possible to refine the analysis and to indicate how these amounts are tending to change over time. At present, data from the first wave only, conducted in 1994, are available which relate to amounts received from both benefits and earnings during 1993. The data exclude Austria, Finland and Sweden, which did not participate, as well as, in part, the Netherlands, for which there are incomplete figures for 1993.

In order to estimate the relationship between benefits and earnings from the data, the analysis has to be restricted to those who were both unemployed and in full-time employment (defined as 30 hours a week or more) for at least part of 1993 (using the data from the ECHP on employment status of respondents during each month of the year). This enables the actual amount each person included in the panel received in the form of unemployment compensation (social assistance as well as insurance benefits) to be compared with their net earnings from work, in each case calculated on a monthly basis (see Box for details). To avoid possible distortions arising from cases where the person concerned is unemployed for only a very short period of time and may not have had time to claim benefit, the analysis is further confined to those unemployed who were out of work for at least three months.

According to the ECHP, around a quarter of men aged 25 and over in the Union who were unemployed for at least three months during 1993 and in full-time employment for one month or more received no unemployment-related benefit at all (though they may have received transfers not linked to unemployment, such as minimum income allowances or even disability or sickness benefits). For those aged under 25, the figure was around a half. The proportion receiving benefits, however, varied markedly between countries, from virtually all men of 25 and over in Belgium, Denmark, Germany, Ireland and the UK to only around a third in Greece, Italy and Portugal (Graph 46). There was even more variation for men under 25, with under 20% of these receiving benefits in Greece, Italy and Portugal.

On average, a slightly lower proportion of women aged 25 and over who were unemployed received compensation than men (just over two-thirds overall), though the figure was significantly less in Germany, Greece, Spain. Portugal and the UK (for those under 25, there are too few observations for most countries to give reliable results) (Graph 47).

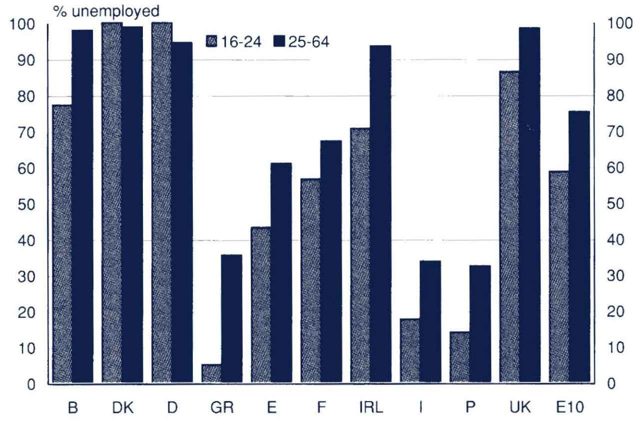
In a number of Member States, therefore, the benefit system does not seem to represent any disincentive at all for many of the unemployed to look for work since they are apparently not entitled to benefit, though it should be emphasised that some of them may be eligible for other kinds of income support not related to unemployment. The disincentive is particularly weak as regards those under 25, who are less likely to qualify for either unemployment-related compensation or other kinds of support.

In terms of the amount received by the unemployed entitled to benefit, the monthly payment to men aged 25 and over averaged around 45% of their net monthly earnings when they were working, which, it should be stressed can be in the job they moved into after being unemployed as well as the one they were in before becoming unemployed. This figure, however, ranged from 77% in Portugal (though the relatively small proportion receiving benefit should be kept in mind) and over 60% in Ireland, Denmark and France to only around 25% in Greece and the UK, with the rate in Italy being just below the Union average, that in Belgium and Germany being just above (at around 50%) and that in Spain, much further above (at 57%) (Graph 48). For those under 25, the number of people covered is in most countries too small to give reliable estimates, though in Denmark, Spain, France and Ireland, where the number is sufficiently large, the replacement rate was similar to that for the older age group.

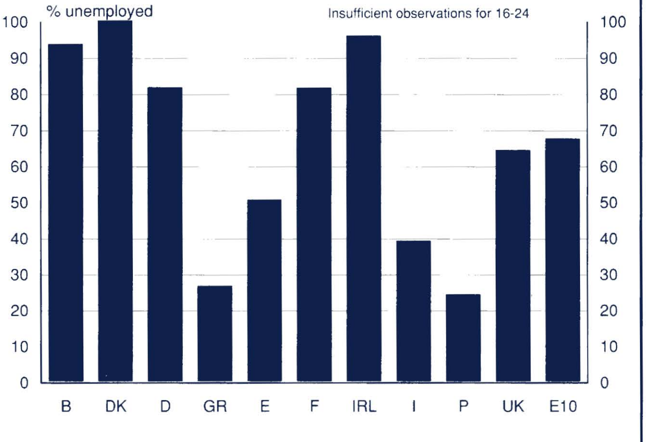
For women, benefit levels in relation to earnings were, for the most part, slightly higher than those for men (at just under 60% for the Union as a whole), though not in Belgium, the UK, Spain, Ireland and Portugal. This may to some extent be a consequence of the fact that women earned less than men when working (about 25% less so far as the total sample was concerned) and though in many cases the rate of benefit is related to previous earnings, payments to women may be less likely to be subject to a ceiling. It could also be that the jobs taken up by women after being unemployed had lower rates of pay in relation to benefit levels than those taken up by men.

These figures need to be interpreted with some caution, not only because the people concerned may be receiving other transfers which are not specified and because the earnings from employment with which benefits are being compared can be either before or after the spell of unemployment, but also because they leave out of account benefits in kind, such as housing allowances. These are important in some countries, such as the UK, where for some recipients they increase significantly the effective amount paid (since those drawing benefits are eligible to have at least an average amount of rent paid by the state in the UK, in addition to local taxes, this can sometimes double the

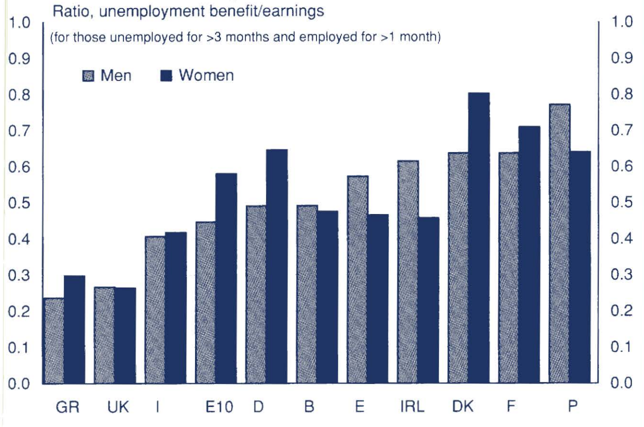
46 Proportion of men unemployed receiving benefit by age group, 1993



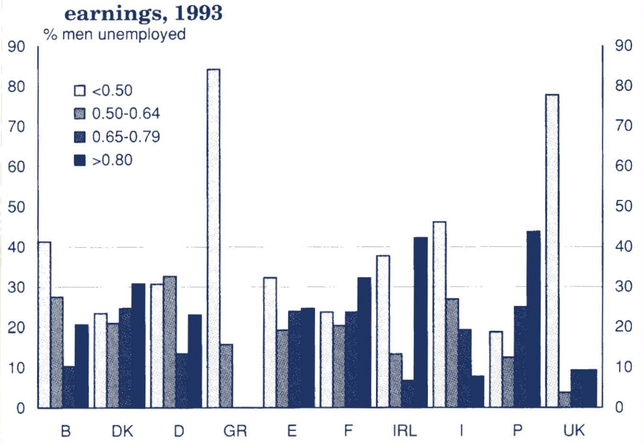
47 Proportion of women unemployed aged 25-64 receiving benefit, 1993



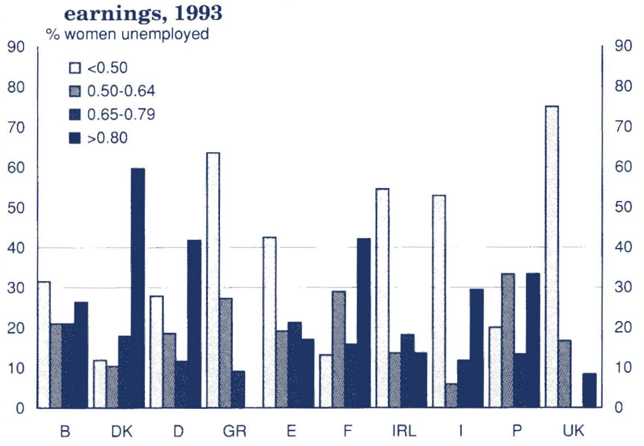
48 Average unemployment compensation relative to earnings for men and women aged 25-64 in Member States, 1993



49 Proportion of men aged 25-64 unemployed by unemployment compensation relative to earnings, 1993



50 Proportion of women aged 25-64 unemployed by unemployment compensation relative to earnings, 1993



effective net income received). Since, however, such benefits relate to households rather than individuals (payment depending on household rather than personal income), they are difficult to take into account. Moreover, since they are also payable in many cases to those on low incomes who are working (along with other in-work benefits for those with children in the UK and Ireland), they have a relatively small effect on the comparison of relative income levels in the case of low paid workers (or those whose potential earnings from employment are relatively low), who account for a high proportion of the unemployed (in the Union as a whole, average wages of those unemployed for at least three months during 1993 were around 20% lower than those of all workers — see Box).

Nevertheless, while the average level of benefits relative to earnings might indicate that overall the financial incentive to be unemployed rather than in work is relatively small in all Member States, the average could potentially conceal wide variations between people. In other words, the distribution of benefit levels is as important in this context as the average. In practice, however, in most Member States, there seem to be comparatively few instances where benefits are so high that they might represent a substantial financial disincentive for those concerned to be in employment. Only in Ireland and Portugal was the proportion of transfer recipients with benefits of 80% or more of net earnings from work over 40%, which in the case of Portugal, given the small numbers receiving benefit, implies that only some 14% of the unemployed fell into this category (Graph 49). In Denmark and France, just under a third of benefit recipients had transfers of 80% or more of earnings, while in all other Member States, the figure was less than a quarter, and in Greece, Italy and the UK, under 10% (zero in Greece). Moreover, in all countries, apart from Portugal, Denmark and France, for over half of benefit recipients, the amount received in transfers relative to earnings was less than 65%.

Much the same is true for women, though in this case, there are three countries — Denmark, Germany and France — where for over 40% of those receiving benefit the amount obtained was 80% or more of earnings (in Denmark, some 60% of recipients), and two — Italy and Portugal — where around a third did (Graph 50). In Greece and the UK, as for men, the great majority of women had benefit levels of under 65% of earnings and in all countries, apart from Denmark, Germany and France, over half did.

Furthermore, in all Member States, the dominant cause of high benefit levels relative to earnings was low wages when in work. Not only did those who experienced a spell of unemployment in 1993 have lower wages on average than those who were employed throughout the year, but the wages of those with high benefit levels in relation to earnings were particularly low. Denmark apart, in all countries the average earnings of men with benefits of 80% or more of earnings were under 60% of the average for all men, and in Belgium, Ireland, Italy and the UK, well under 50% of the average (Graph 52). For women, average earnings of those with high benefits in relation to earnings were less than

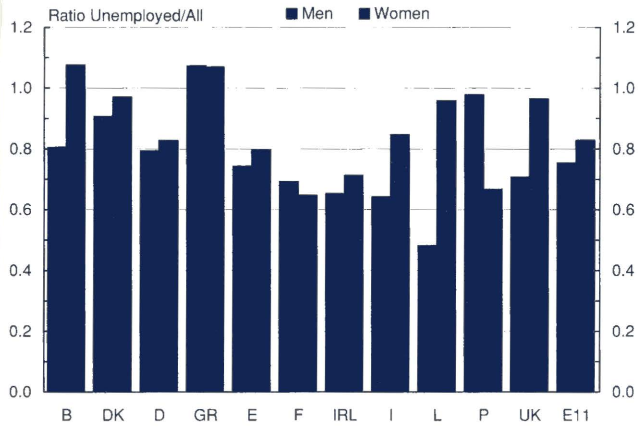
The pay levels of those experiencing a spell of unemployment

For the Union as a whole, the monthly net earnings of both men and women aged 25 to 64 experiencing a spell of unemployment in 1993 were significantly lower than those of all employees (25% lower for men and around 17% lower for women). This is broadly consistent with the evidence (from the Community Labour Force Survey) that the educational attainment levels of the unemployed tend to be significantly lower than for the rest of the work force. (In terms of gross earnings, moreover, the difference is likely to be wider given the progressive nature of the tax system in most countries.)

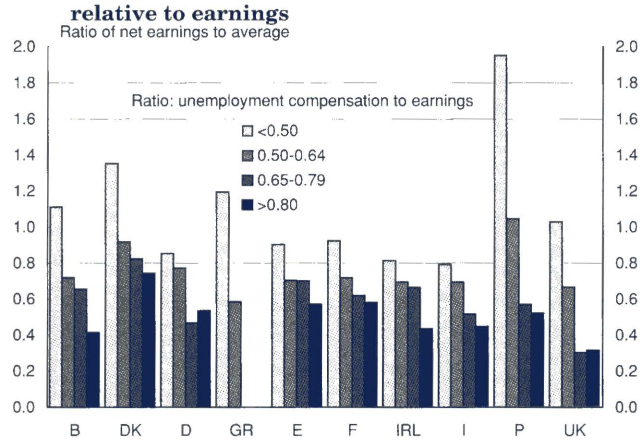
In the case of men, only in Greece, did those unemployed for part of the year have higher monthly earnings in the period when they were working than men as a whole, though in Portugal, their earnings were much the same (Graph 51). This perhaps reflects the narrow coverage of unemployment benefits in the two countries, as well as the fact that educational levels of the unemployed are less different from others in the labour force in both countries than in other parts of the Union. These two countries apart, except in Denmark (where the difference was only around 10%), the net earnings of men experiencing unemployment were at least 20% lower than average earnings (in Belgium and Germany) and some 30% or more lower in France, the UK, Ireland and Italy (50% lower in Luxembourg, though the sample size is relatively small). This pattern reflects perhaps the relatively wide dispersion of earnings in France, the UK and Ireland and, seemingly, the relatively low skill levels of those receiving unemployment benefits in Italy.

In the case of women, average monthly earnings during the time they were in work of those unemployed for at least three months and drawing benefit were closer to average earnings of women employees as a whole in all Member States except France and Portugal. In Belgium and Greece, they were higher — which in the former case, is difficult to explain given the much lower educational attainment levels of women unemployed than those of the rest of the work force. In Denmark and the UK, as well as Luxembourg, they were under 5% lower than for all women, which in the UK, at least, might reflect the relatively small difference in education levels between the unemployed and other members of the labour force.

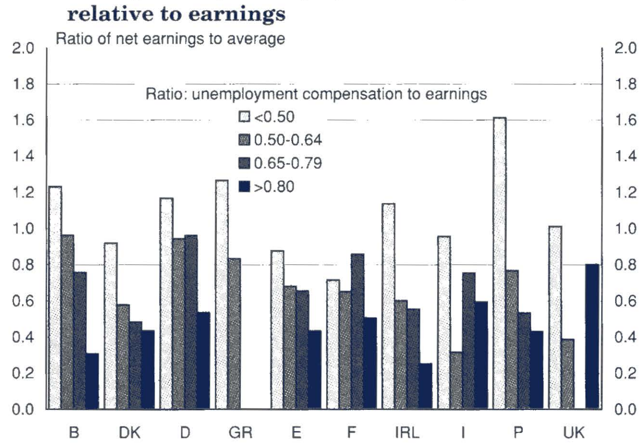
51 Relative wages of men and women unemployed for 3 months during 1993



52 Net wages of men experiencing unemployment during 1993 by unemployment compensation relative to earnings



53 Net wages of women experiencing unemployment during 1993 by unemployment compensation relative to earnings



60% of average in all countries except the UK (where for only 8% of benefit recipients, the amount received was 80% or more of earnings) and in all others except Germany, France and Italy, well under 50% (Graph 53).

In sum, the evidence does not suggest that benefit levels are especially high in relation to earnings from employment across the Union for most of the unemployed and where they are, the cause lies in the low wages which those experiencing unemployment tend to be paid rather than in generous levels of benefit. Indeed, in most Member States, for those whose earnings are close to the average, the benefits they receive when out of work are likely to be only around half of their net pay when in work.

Finally, in most Member States, as noted above and as described in more detail below, changes have been made to unemployment compensation systems since 1993 which have had the effect either of reducing benefit levels further or restricting entitlement, so that levels in relation to earnings and the proportion receiving payment may well be lower now than indicated here.

Disincentive effects

Any assessment of the scale of disincentive effects on employment associated with particular benefit systems needs to recognise that financial considerations alone are not the only factor determining whether or not a person chooses unemployment over working. Quite apart from the various controls restricting eligibility for benefit —

stipulating, in particular, that the person concerned must have left their previous job involuntarily, must be actively looking for work and, before too long, must accept any reasonable job offer — there are a range of non-financial advantages from working which can mean that someone will prefer to have a job rather than be unemployed for much the same income. These advantages have been emphasised in the debate on social exclusion, which has drawn attention to the problems of lack of self-fulfilment and marginalisation, or a sense of not belonging, which comes from being out of work.

At the same time, it is far too simplistic to reduce the effect of benefit systems on the labour market to a question of incentives to look for work. In particular, the nature of systems is likely to influence:

- the extent of labour mobility between jobs, as noted above, insofar as it provides more or less protection against the risks of becoming unemployed associated with such moves;
- the willingness of people to take jobs with fixed-term contracts;
- negotiations between employers and employees over possible redundancies and the ease with which workers can be dismissed;
- the willingness of people, especially women who have stopped working to take care of children, actively to look for work and to retrain.

As such, effectively designed benefit systems can improve rather than obstruct the functioning of labour markets and can increase the competitiveness of the economy rather than damage it.

Main reforms: the shift from passive to active policies

In principle, the distinction between passive measures of income support and active measures to help people find a job is clear, and there is a growing consensus across the Union about the desirability of shifting from the former to the latter. In practice, however, the distinction is often blurred. Training or socially-useful employment schemes can, for example, sometimes be aimed primarily at providing income support — and perhaps reducing the unemployment figures — rather than improving the employability of participants, while subsidised employment can be a means of supporting firms in decline rather than of increasing net job creation. At the same time, income support can become an integral part of an active programme for getting people into work.

The relationship between passive and active measures can take three forms:

- active measures are aimed at establishing individual programmes to help benefit recipients get back into work;
- unemployment compensation is used to provide financial support for access to employment;
- unemployment compensation is conditional on the recipient taking up a specially created job outside the normal labour market (workfare).

These are analysed in turn below.

Active measures to support job search

Increased efforts have been made in many parts of the Union to help the unemployed find a job, though this has been coupled with increased pressure on them to do all they can themselves. On the one hand, public employment offices have improved their placement services and the counselling and guidance given to the unemployed, which now often include assessment of skills and identification of suitable training courses to enhance these. On the other hand, continued payment of unemployment benefits has been made conditional on participation in active labour market programmes or the acceptance of a suitable job offer.

In Denmark, for example, the period of entitlement to benefit has been divided into two phases, the second of which is focused on active programmes which the person concerned is required to participate in (see Box on Denmark). In the UK, since the introduction of the Jobseeker's Allowance, the unemployed are required to enter into an agreement with the employment services, detailing the steps to be taken for them to get back into work (see Box on the UK). Similarly, in Belgium, the unemployed over 46 and with low skills are obliged to sign much the same kind of contract with the regional employment services, committing themselves to participate in active programmes or have their benefits withdrawn.

Active programmes, however, tend to be costly and when faced with sharp rises in unemployment, it can be difficult to maintain adequate numbers of places. In Sweden, for example, while in principle, all the unemployed are entitled to training or to a socially-useful job after a given period out of work, the extent of the economic recession at the beginning of the 1990s made it impossible, in practice, to do this. Expenditure on passive measures of income support, therefore, rose from under 30% of the total in 1989 to over 50% in 1996. In the latter year, a new programme was introduced aimed at halving unemployment by the year 2000 (from 8% to 4%), while a debate was initiated on whether those on training courses or in socially-useful employment should any longer be entitled to insurance benefit, bringing the Government into conflict with trade unions.

The cost of active measures is the main reason why, despite the increasing importance attached in Member States to the provision of training to improve the employability of those out of work, comparatively few of the unemployed at present receive training, which tends to be provided in most cases only after they have been unemployed for some time. The European Council in the conclusions to the Luxembourg Job Summit at the end of 1997 emphasised the importance of improving the situation in this respect and the Employment Guidelines agreed by the Council at the beginning of 1998 set the objective of doubling the proportion of the unemployed receiving training over the next few years.

Denmark: the activation of policy

The relatively generous unemployment compensation system has been modified since 1993 in a series steps aimed at tightening eligibility criteria and reducing the duration of benefits, while giving more help to recipients to find work and so strengthening the articulation between passive and active measures.

Specifically, the minimum employment record required to qualify for unemployment benefit has been raised from 26 to 52 weeks over preceding three years, while the maximum duration of payment has been reduced progressively from 9 years to 7 and then to 5 — though those over 50 can, under certain circumstances, continue to receive benefits until they are 60. During the last three years of this period, efforts to get the person concerned into work are intensified and they have a right to training or subsidised jobs, though they also have an obligation to accept what is offered in this regard. Even over the first two years, however, a substantial amount of assistance is provided to help with job search and to improve employability, an individual plan tailored to their needs being drawn up after three months to define the action to be taken.

In 1995, the definition of what constitutes a suitable job offer was extended to cover any type of work which the person is capable of doing with a minimal amount of training and sanctions were introduced for those refusing such an offer.

Those who have particular difficulty in finding work can, since 1996, be offered part-time jobs in socially-useful activities for up to three years, while effectively continuing to receive unemployment benefit.

Unemployment compensation to support access to employment

In virtually all Member States, various schemes exist to subsidise the employment of someone who is unemployed, either by providing direct grants to companies taking them on or relieving them of some or all of the social contributions normally payable. More recently, a slightly different form of scheme has been introduced in some countries involving the transfer of unemployment benefits to employers as an inducement to recruitment.

In France, businesses which employ a benefit recipient who has been out of work for more than 8 months receive a subsidy equal to, or higher than, the total amount the person would have received in benefits up until the end of their entitlement period.

In Italy, workers made redundant by businesses subsidised through the *CIG* (see below) receive mobility benefits for between 12 and 48 months (according to age and region). Firms recruiting these people to a permanent job are then eligible for a subsidy equal to half the mobility benefit which is still outstanding.

In Germany, 'productive salary subventions', introduced in 1993 in the new East German Länder and extended in 1994 to the rest of the country, are payable to employers who take on people unemployed with special problems, the amount being determined by the average value of benefits which they receive.

In Austria, a special subsidy was introduced in 1997 to employers taking on those who have been out of work for over 6 months and who cannot get a normal job. This lasts for up to a year and is equivalent in value to the unemployment benefit plus the pension and health contributions payable.

At the same time, measures have also been introduced in a number of Member States to encourage the unemployed to accept low-paid or part-time jobs by allowing them to continue receiving benefit, so, *inter alia*, alleviating any 'unemployment trap' which might exist because of potential earnings being little or no higher than unemployment benefit.

In Belgium, benefit recipients who accept a part-time job receive an additional amount to ensure that their total income when working is higher than the normal (full-time) unemployment benefit.

In Germany, anyone who is unemployed and receiving benefit can have an allowance added to their salary if they accept a fixed-term (of up to 3 months), low-paid job. In Finland, tax incentives were introduced in 1997 to encourage the unemployed in receipt of benefits to take up part-time or short-term jobs (by reducing the amount of tax payable on the combined income). In Portugal, a recently-introduced measure allows the unemployed to work part-time and to receive a partial benefit (rather than no benefit at all). In Ireland, a *Back-to-Work-Allowance* is payable for three years (at a declining rate of 75%, 50% and 25% of their benefit) to those who are unemployed and 23 or over who take a job of 20 hours a week a more. (In 60% of cases, this has been used by the recipient to set up as self-employed.) In the UK, people unemployed for over 3 months who accept a part-time job are entitled to a *Back-to-Work Bonus*, while a *Jobfinder's Grant* is payable to those unemployed for over two years who accept a job paying less than a given amount.

In both the latter two countries, in-work benefits are also payable to

The UK: the activation of policy

In the UK, the articulation between income support for the unemployed and active policies to get them back into work has been taken further than anywhere else in the Union. Since 1982, unemployment benefits have been flat-rate and payable for one year, up to the introduction of the Jobseeker's Allowance in 1996 and 6 months thereafter. After this period, payment remains at the same rate but becomes means-tested (in relation to household income).

During the 1990s, a number of measures were introduced to restrict entitlement to benefit, including the exclusion of young people under 17, a tightening of eligibility criteria and the gradual erosion of the value of benefits in relation to earnings, before the introduction of the Jobseeker's Allowance to encompass both unemployment insurance benefits and social assistance. In addition to halving the benefit period to 6 months — the shortest in the Union — and thereby increasing the number dependent on means-testing, the new system requires everyone claiming benefits to enter into a Jobseeker's Agreement with Job Centres (the employment services), defining their rights and obligations and setting out the steps to be taken to find a job. The employment services have developed a range of programmes which apply after someone has been unemployed for 13 weeks, 6 months, a year, 18 months and 2 years, and which consist of various measures including guidance on job seeking techniques, evaluation of skills, training, work experience and, for those under 25, socially-useful jobs.

Although participation in programmes is voluntary, entitlement to benefit can be suspended if it the person concerned is not sufficiently cooperative or considered not to be making sufficient effort to look for work or improve their skills. In addition, while job seekers can turn down job offers during the first 13 weeks of unemployment if the qualifications required are significantly different or lower than those involved in what they were doing before or if the salary is less, after 13 weeks, these may no longer be regarded as just cause for refusal and after 6 months, they are obliged to accept any job they are capable of doing, irrespective of the level of pay.

people employed in low-paid jobs, the purpose being to increase the financial gain from taking up such a job as compared with remaining unemployed. In Ireland, a *Family Income Supplement* was introduced in 1984 with the aim of compensating someone moving into a low-paid job after being unemployed for the loss of child allowances included in unemployment benefit, the amount payable varying inversely with earnings. From 1996, it has also become payable to single people and couples with no children.

In the UK, *Family Credit*, was introduced in 1988, to provide additional income to people with children working in low-paid jobs for at least 16 hours a week. As in Ireland, the amount varies inversely with earnings and for the large majority of people ensures that disposable income from working is higher than the amount receivable when unemployed. As such, it helps to avoid the interaction of the benefit system and the wages on offer to those out of work creating a so-called unemployment trap, where there is little or no financial gain from working. The cost, however, is the creation of a poverty trap, where those receiving in-work benefits find it difficult to improve their position because of the withdrawal of benefits as their earnings increase (the benefits withdrawn include not only Family Credit but also housing benefits and council tax relief). Since October 1996, a similar allowance, *Earnings Top-Up*, has become payable on a trial basis to those without children.

Towards workfare?

In recent years, a new debate on 'workfare' has taken place, the case in favour essentially being that those receiving unemployment benefit should do something in return, or at least accept some obligation towards society for what they are being paid. An element of workfare is evident in the increased obligation imposed on the unemployed in many countries to accept jobs that they are offered and in the broader interpretation attached to the suitability of such jobs. It is also evident in the increased obligation on them to participate in active labour market programmes, such as vocational training courses. In general, however, workfare is usually interpreted more narrowly to mean a requirement to work, typically on socially-useful projects, in order to continue to receive benefits.

Workfare programmes can be beneficial for participants, in that they enable them to have a job and to maintain or develop new skills and so improve their chances of getting back into normal work. On the other hand, they also risk institutionalising inferior forms of employment. Whether the former or latter view is the more valid depends on the content of the jobs concerned, on the way they are organised and on what subsequently happens to participants. In most cases, the schemes now operational in Member States are of too recent origin to allow a judgement to be made one way or the other.

In Belgium, a scheme to provide socially-useful work to the long-term unemployed has existed since 1987, though it was modified considerably in 1994. It is organised by local employment agencies set up by communes and is at present targeted on those out of work for over three years, or two years in the case of school-leavers, who have 'a right and duty to participate', who can be employed for up to 45 hours a month without a work contract and who receive an additional allowance on top of their unemployment benefit.

In the Netherlands, as part of the reform of the minimum income guarantee system in 1995, municipalities were charged with introducing a scheme to provide socially-useful activities for benefit recipients, who are not paid any extra for participating but who can have their assistance reduced or suspended if they refuse to do so. Pilot schemes are currently being tested in 25 cities, and up to now, instead of sanctions being applied to those refusing to join, there have been financial incentives to participate.

In Sweden, as a temporary measure in 1997 and 1998, the public sector has been allowed to offer jobs of limited duration (9 months at most) to unemployment benefit recipients, who receive a supplement of 10% to their benefit and are able to spend 10% of their time looking for a normal job.

In Ireland, a scheme was launched in 1997 to enable those out of work for more than 6 months and at risk of becoming long-term unemployed to work in a company for 5 weeks, while retaining their benefit and receiving an allowance to cover their travel costs to and from work.

Similarly, in the UK, those under 25 and unemployed for more than 6 months are eligible for the *Work Trials* programme, which gives them a job for 3 weeks and continued entitlement to benefit.

At present, refusing to participate in these kinds of programme does not seem, in general, to invoke sanctions, though in most cases, the possibility exists of withdrawing income support. Whether participation serves to increase the employability of the person concerned, however, is so far an open question, since there is as yet no systematic evidence available on what happens to them after they come off the scheme.

It is also open to question how much of a shift from passive income support to these and other kinds of active measure can be achieved without adding to overall expenditure. The provision of socially-useful jobs is not costless, despite the fact that participants in many cases receive no more, or not much more, than their unemployment benefit. This also holds for the provision of training courses, counselling, guidance and other help with job search which may increase the chances of those out of work finding employment, but until they do, such measures add to the cost of income support. Measures to subsidise employment, on the other hand, seem at first sight to offer the possibility of keeping down expenditure, especially where subsidies are being paid out of benefits. This assumes, however, that the jobs being created are entirely additional, that those filling them add to the numbers in employment, and that there is no displacement of existing jobs or existing workers. In practice, this is a very strong assumption to make and, on past evidence, one which is not realistic.

Subsidies to take on particular groups of workers are almost certain to result in the displacement of others, however the scheme is organised, and the net effect in increasing employment is likely to be much less than the number of jobs, or people, being supported. Nevertheless, even if the net effect were to be zero, it would still mean that the average duration of unemployment among the targeted groups were reduced and that they have an opportunity to gain work experience, which is arguably preferable to leaving them to suffer prolonged unemployment and social exclusion.

In practice, the expenditure implications of shifting from passive to active measures, especially in a context of rising unemployment, has tended to limit the change which has taken place. Over the Union as a whole, as detailed below, the share of expenditure going to active measures in 1996 was marginally lower than in 1990, though slightly higher than in 1993 at the end of the period of economic recession. At the same time, the greater weight given to active measures, allied to the rise in unemployment during the recession years, has tended to reinforce efforts to curb expenditure on income support, if only to prevent the overall share of resources going to the unemployed from increasing. In a context of constraints on social expenditure, in other words, it is likely to be difficult politically to justify spending more on active programmes to help the unemployed without reducing what they receive in other ways, quite apart from the desire to strengthen the financial pressure on them to find a job.

Accordingly, Governments across the Union have sought means of reducing expenditure on passive measures, without cutting income support to unacceptable levels. In many cases, this has led to a focus on tightening eligibility and shortening the duration of benefits as well as on the level of support itself.

Restricting entitlement to benefit

Qualifying conditions for entitlement to benefit have been tightened in most Member States over recent years, in some cases as a means of supporting relatively generous benefit levels, and, in a number of countries, the employment record required for eligibility for benefit has also been extended. Moreover, there has also been a tendency to shorten the period of entitlement to benefit and to reduce the amount received as the duration of unemployment lengthens. The only exception is in Italy, where after the reform of the *CIG* (the system of income transfers to workers on lay-off which had become the main means of paying unemployment compensation — see below), the standard unemployment, benefit was raised from $7^1/_2$% of previous earnings in 1988 to 30% in 1994 and, prospectively, to 40%, though the agreement on this reached in 1995 has still to be implemented.

In two other Member States, however, France and Sweden, there has been some recent relaxation of the restrictive measures implemented during the recession of the early 1990s. Before then, the unemployment benefit system in Sweden had been the most generous in the Union, with a benefit rate of 90% of previous earnings. This was reduced to 80% in 1993 and to 75% in 1996 before being increased again to 80% in September 1997, while the minimum employment record for eligibility has been increased twice over the 1990s. Moreover, in Italy, where expenditure on unemployment benefits *per se* is among the lowest in the Union, recommendations were made in the Onofri Report, published in February 1997, for the consolidation of the present fragmented arrangements into two unified schemes, one providing insurance benefits for three years to the 'fully' unemployed at an initial rate of 60% of previous earnings, but declining as the period of unemployment goes on, and the other providing benefits to those on lay-off for 12–18 months in any 5 year period, also at a declining rate, though starting at 70% of previous earnings.

Nevertheless, in general, the restrictive measures adopted during the economic recession have been maintained in Member States. In Germany, measures introduced in 1994, and subsequently modified in 1997, as part of legislation for promoting employment (*Arbeitsförderungsgesetz*) have restricted entitlement to benefit and reduced the rate from 63% to 60% of previous net earnings (for those with no children and from 68% to 67% for those with children). In addition, social assistance, payable after one year and the expiry of the period of eligibility for insurance benefits, was reduced from 56% of previous net earnings to 53% (and from 58% to 57% for those with children). The tightening of eligibility conditions coupled with the increasing number of long-term unemployed has led to fewer people receiving insurance benefits since 1993 and more receiving social assistance.

In Belgium, where because of lax eligibility criteria, virtually all the unemployed used to qualify for insurance benefits and often for unlimited periods of time, conditions for entitlement have been tightened during the 1990s, mainly for young people of 25 and under, while the waiting period for benefit has been lengthened considerably. Moreover, attempts have been made to limit the duration of entitlement to benefit, especially in the case of those living in the same house as someone in work, by introducing the possibility of withdrawing benefit if the person concerned has been out of work for $1\frac{1}{2}$ times the average duration in the region where they live. (In 1996, some 61% of the unemployed in Belgium had been out of work for a year or more, 40% for two years or more and 22% for at least 4 years, all the figures being significantly higher than the Union average and the last figure, almost twice as high.) In addition, the level of benefit has also been reduced, though the minimum amount has been maintained.

In Spain, the unemployment compensation system was tightened in 1992, the period of contributions required for eligibility for benefit being increased from 6 to 12 months, the duration of entitlement (proportional to the contributions paid) being reduced by a third, on average, and the level of benefit being cut by 10% of previous earnings (from 80% for the first 6 months to 70% and from 70% for the next 18 months to 60%). As a result, expenditure on income support of the unemployed fell by a third in real terms between 1993 and 1996 while the number unemployed remained much the same (this is consistent with the ESSPROS data analysed in Chapter 3). Nevertheless, expenditure on active measures accounted for only just over $\frac{1}{2}$% of GDP in 1996, less than in 1990. Moreover, no direct link exists between active programmes and the system of income support.

In Greece, the system of unemployment compensation was already among the least generous in the Union before 1996, when the previous scheme, under which benefits payable for up to a year at a rate of 50% of previous earnings in the case of industrial employees and managers and 40% in the case of other workers, but up to a maximum of only two-thirds of the minimum wage, was replaced by a lump-sum of half the minimum wage.

In Finland, where a universal system of unemployment compensation combining insurance benefits payable for a fixed period with a basic allowance payable indefinitely had been developed over the 1970s and 1980s, restrictive measures were introduced in 1994, requiring a person to have been employed for at least 6 months during the previous two years to be eligible for benefit and limiting payment of benefits to 500 days in 4 years. In 1997, the period of employment was increased to 10 months and benefits were made proportional to earnings during these 10 months, so reducing the amount payable significantly. In addition, benefit amounts have been further reduced by their non-indexation in 1995 and 1996.

Maintaining the right to benefit

In most Member States, the conditions governing entitlement to unemployment benefit have also been tightened. Not only have controls against unjustified claims been strengthened in many cases, but the unemployed have also been put under increased pressure to accept suitable job offers.

In many countries, the fight against abuse of the system has been intensified by establishing or reinforcing specialised agencies and by improving the exchange of information between the organisations involved in benefit payment. In the Netherlands, legislation was introduced in 1997 enabling transfers to be suspended, fines imposed and repayment of benefits required in cases of wrongful claims. In Denmark, a special unit was established in 1996 to monitor the action taken by insurance funds in relation to those turning down jobs or refusing to participate in active labour market programmes. In the UK, control of abuse has been reinforced by requiring the unemployed to have closer contact with the employment services and to demonstrate that they are taking steps to find a job.

At the same time, the definition of what constitutes a suitable job offer has been widened in a number of Member States. In the UK, the concept of a 'suitable' job offer was replaced in 1989 by a requirement that, after the first 13 weeks of being unemployed, the person concerned had to accept an offer unless they had 'good cause' to refuse it. Whereas for the first 13 weeks, they are able to turn down a job if it does not correspond to their qualifications or previous earnings, after this period, this ceases to be regarded as being 'good cause' for refusal.

In Belgium and the Netherlands, after someone has been out of work for 6 months, they are required to accept a job even if it involves a lower skill level than the one they were doing before. In Germany, the unemployed are classified according to their qualifications and can refuse a job if it does not correspond to their classification. As their spell of unemployment lengthens, however, they are reclassified to a lower level of qualifications. Legislation introduced in 1997 specifies that it is acceptable, during the first three months of unemployment, for earnings to be reduced by 20% in relation to what they were previously receiving and by 30% during the following three months. After 6 months, people are required to accept any job offer, even at a wage lower than the level of unemployment benefit.

In Austria, a new interpretation of 'suitability' was introduced in 1993 to cover any job which does not endanger the chances of the person concerned being able to resume the type of work they were doing before. For those on social assistance, a job is regarded as suitable if it is considered that nothing more suitable is likely to emerge in the near future.

The effect of all these measures should be to increase the flow of people out of unemployment and into work or into active labour market programmes and, therefore, to reduce the average duration of unemployment, though not necessarily the number unemployed at any point in time, as noted above. However, although long-term unemployment seems to have fallen in relation to overall unemployment, it remains high and it is difficult to ascribe all of the fall to these kinds of measure. (In 1996, some 48% of the unemployed in the Union had been out of work for a year or more, slightly down from 49% in 1995, but up from 43% in 1993. The proportion in 1996, however, was lower than in the mid-1980s, when it was as high as 55% and when it was associated with a slightly lower overall rate of unemployment. The relationship between long-term and overall unemployment, therefore, seems to have improved over this 10 year period, though how much this is due to changes in compensation systems as opposed to active measures, or, indeed, other factors, is unclear.)

Relationship with other measures

As noted above, there are other means than unemployment benefits to support the income of the unemployed. As also noted, there was tendency up until recently to shift people from unemployment benefit to other types of support, early retirement schemes and disability benefits, in particular. In some countries, moreover, special measures were introduced to compensate people who were on lay-off — ie temporarily unemployed — or working short-time. These various kinds of scheme are considered below, beginning with the latter type of arrangement.

Partial unemployment

The most significant example of a partial unemployment scheme is the *CIG* (*Cassa Integrazione Guadagni*) in Italy, which, in principle, provides compensation to those who remain in employment but who are on lay-off for a temporary period. In practice, however, until recently at least, this period could extend for number of years and the scheme effectively assumed the role of normal unemployment benefit systems in other countries (see Box on Italy).

In France, under the *5-year Employment Act* of 1993, companies are able to receive compensation for part-time or temporary unemployment for up to a maximum of 1200 hours over an 18 month period (ie for just under half-time working). In Germany, the partial unemployment compensation scheme (*Kurzarbeitgeld*) was extended from 6 months to 24 months to assist industrial restructuring in the new Länder after unification and has subsequently been widened to cover the whole country.

Italy: the reform of Cassa Integrazione Guadagni (CIG)

The CIG, created soon after World War II, consists of two schemes — the ordinary scheme (CIGO) to provide assistance in the event of partial or temporary redundancies and the special scheme (CIGS) for industrial restructuring. Compensation in both cases amounts to 80% of previous earnings up to a maximum sum and initially could be paid for indefinite period, though in 1991 it was limited to two years. Since the workers concerned continue to have a formal contract of employment, they are not classified as unemployed (under the ILO definition, they are neither actively seeking work nor available for work).

At the end of the 1980s, the schemes were heavily criticised for maintaining fictitious jobs to the benefit of certain workers — those in industry — at the expense of others — those in SMEs. In 1991, the system was reformed, not only by limiting the duration of benefits, but also by imposing some of the cost of financing it on to employers, making a clearer distinction between those supported by the scheme and redundant workers and introducing a mobility allowance for the latter to give employers a financial incentive to take them on, and stipulating that those on CIG must rotate (though firms seem to prefer paying fines than to comply with this requirement).

Nevertheless, because of recession, the CIGS was extended in 1993 and 1994 to SMEs and certain services.

Early retirement

As noted in Chapter 2, policy towards early retirement has been modified in a number of countries in recent years in response to both the growing cost and demographic trends. In many cases, it is still the case that older people (especially those aged 55 and over) who are unemployed and drawing benefits are treated differently than younger ones in the sense that they are under less obligation, or no obligation at all, to look for work. Nevertheless, in some countries, special early retirement schemes have been withdrawn, people are being encouraged to remain in work rather than leave the labour force prematurely and, if they do, attempts are being made to ensure that they are at least replaced in their job by someone else.

In Austria, older workers (women of 54 and over and men of 59 and over) used to be able to receive a special allowance (*Sonderunterstützung*) of 80% of previous salary under the unemployment benefit scheme if they took early retirement. This provision, however, was withdrawn in 1996 and replaced with a *bonus-malus* scheme, with penalties on companies for the dismissal of older workers and reductions in social contributions for those taking them on, encouraging the continued employment of those approaching retirement age.

In Germany, extensive use of early retirement schemes was made in the past as a means of softening the effect of redundancies. Until 1996, a full pension was payable to those over 60 who had been unemployed for at least a year during the preceding 18 months, those of 55 and over were entitled to unemployment benefits for a 32 month-period instead of a year and anyone unemployed over the age of 58 could receive benefits without having to look for work. Since then, in addition to the gradual raising of the retirement age to 65 for everyone, those who leave their job before they reach this age have their benefit reduced (by an amount proportional to the number of years required to reach the official retirement age). At the same time, as discussed in Chapter 5, a part-time unemployment scheme for older workers has been introduced which provides compensation so long as the person concerned is replaced by an apprentice or someone previously unemployed.

In France, where various schemes encouraging early retirement have been in operation for some time, a new arrangement, financed from the unemployment insurance fund, was introduced in 1995, enabling those under 60, the official retirement age, to stop working so long as they have paid contributions for at least 40 years and so long as their employer undertakes to replace them within 3 months by someone previously unemployed. They then receive a benefit equivalent to 65% of their previous earnings until they reach 60.

In Sweden, where the emphasis of policy is on reducing early retirement, measures were introduced in 1997, first, to enable those aged between 60 and 65 who have been unemployed for over a year to receive unemployment benefit until retirement without needing to look for a job and, secondly, to allow older workers to receive unemployment benefit if they leave their job voluntarily and are replaced by a young person previously unemployed or looking for their first job.

Invalidity benefits

Granting entitlement to invalidity, or disability, benefit was a common way in the past of providing income support over the long-term to those unable to find a job, particularly manual workers in their 50s previously employed in heavy industries, such as iron and steel, ship-building or mining, which declined dramatically during the 1970s and 1980s. While, in principle, eligibility for such benefits was conditional on suffering a disability which restricted the ability to work, in practice, this was often interpreted liberally to include, relatively minor ailments, psychological problems and consideration of local labour market conditions. The result was a significant growth in the number of people drawing invalidity benefits in a number of countries and an escalation of expenditure on these.

The general concern during the 1990s across the Union has been to try to reduce expenditure in this area by making eligibility criteria more stringent. This is has been especially so in the two countries where growth had been particularly marked, the Netherlands and the UK. In both countries, medical examinations of those claiming entitlement have been made more stringent and, to be eligible for benefit, people have to demonstrate that they are incapable of doing any kind of work rather than just the job they were doing before. Moreover, in the Netherlands, as a further means of control, responsibility for payment has been transferred to employers (see Chapter 2, Box on the Netherlands).

Similarly, in Italy, where invalidity benefits were used as a means of providing income support for the long-term unemployed, especially in regions where unemployment rates were high, more stringent conditions on eligibility have been applied during the 1990s and the number of people receiving benefit has declined (by 14% between 1990 and 1994).

The effect of these changes on social protection expenditure is hard to judge. The main consequence may have been to shift people from disability benefit schemes to unemployment benefit or to social assistance rather than to reduce the overall number dependent on social transfers. Although some may have been able to find work, the relatively low rate of employment growth which has obtained across much of the Union since the recession of the early 1990s suggests that job shortages still represent a formidable obstacle to the ability of the people concerned to make the transition from welfare dependency to paid employment.

Changes in expenditure on passive and active measures

It remains to examine the effect of these changes in policy on actual expenditure on passive measures of income support for the unemployed as opposed to that on active programmes to help them into work. According to OECD data (on labour market policy — the ESSPROS module on this has yet to be developed), expenditure in the Union on passive and active measures combined in relation to GDP has closely followed the change in unemployment, or in those needing support. Between 1990 and 1996, overall expenditure went by from $2^1/_2$% of GDP to just under $3^1/_2$% (a rise of 39%), while unemployment increased from $7^1/_2$% of the labour force to just under 11% (a rise of 44% in the number out of work) (Graph 54). After 1993, however, there was a slight fall in spending relative to unemployment. Within total expenditure, the share of resources going to active as opposed to passive measures, remained fairly constant over the 6 years as a whole, at just over a third, though there was some reduction in share in the earlier years when unemployment was rising, followed by some increase as unemployment stabilised.

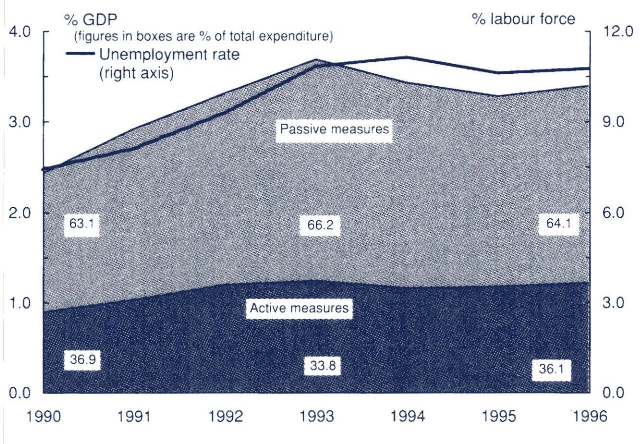
This pattern of change in expenditure during the 1990s has been similar to that which occurred before. In particular, between 1985 and 1990, when unemployment fell, overall expenditure declined by around 1/2% of GDP, slightly less than the reduction in the number unemployed as the opportunity was taken of expanding spending on active measures (this rose slightly in relation to GDP as the number requiring support was falling while spending on passive measures declined broadly in line with this fall).

Although there is a broad similarity in the changes in expenditure which have occurred in individual Member States, insofar as changes in unemployment have been the major factor underlying not only the development of spending as a whole but its division between active and passive measures, there are also some important differences which reflect differential policy efforts. In most Member States, total labour market spending was higher in 1996 than in 1990, reflecting the fact that unemployment was also higher (the only exceptions being Denmark and Ireland where unemployment was lower in the later year) (Table 8). In Greece, Spain and Ireland, however, spending was lower, in Ireland largely because of a lower rate of unemployment, in Greece and Spain, because of lower spending per person unemployed — in Spain, especially in the latter part of the period — largely on passive measures of income support in both cases (Graph 55, where expenditure relative to GDP is expressed in terms of a constant rate of unemployment). Expenditure on passive measures relative to unemployment was also down in France and Belgium, while on active measures, it was down in Finland and Sweden as well as in Germany and Belgium.

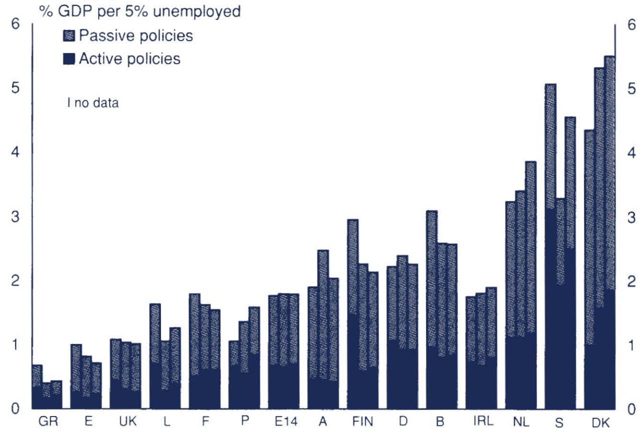
The only Member States where overall expenditure per person unemployed increased relative to GDP over the 1990s were Portugal, the Netherlands and Denmark, in the former two because of higher spending on passive measures, in the last, largely because of increased spending on active policies. Indeed, Denmark was the only country in the Union to show a significant increase in expenditure in relation to GDP over this period (Graph 56). It was, moreover, one of only three countries where the share of expenditure devoted to active measures was higher in 1996 than in 1990, the other two being France, where this was partly a result of a reduction in passive spending per person unemployed (Graph 57) and Ireland, where, as in Denmark, unemployment fell, as noted above.

In contrast, in Germany (Graph 58), Finland, Sweden (Graph 59) and the UK (Graph 60), the share of expenditure going to active measures declined

54 Public expenditure on active and passive labour market measures in the Union, 1990-96

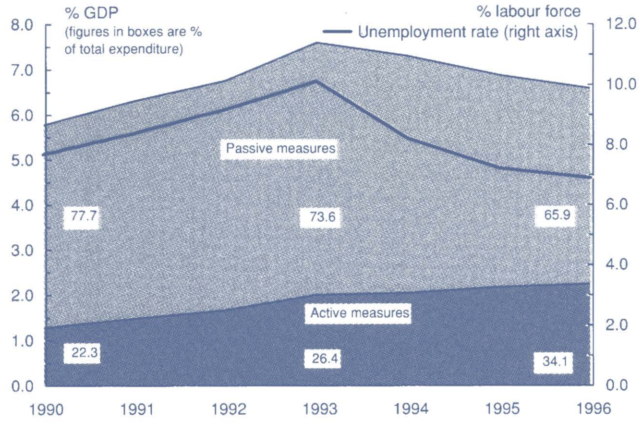


55 Public expenditure on active and passive labour market policies in Member States, 1990, 1994 and 1996

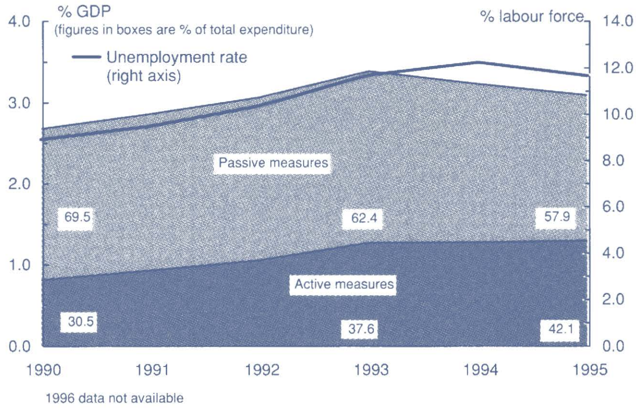


Public expenditure on active and passive labour market measures

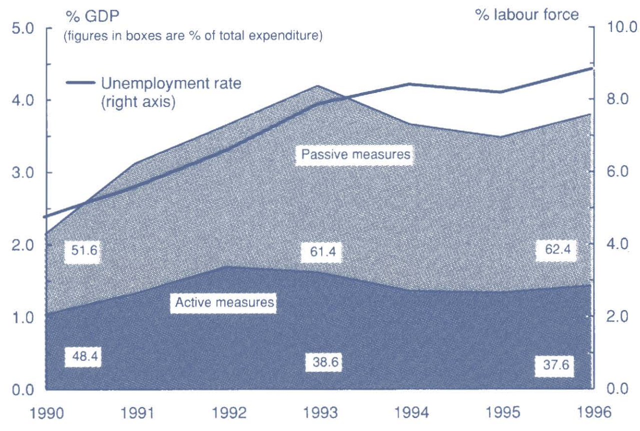
56 Denmark, 1990-96



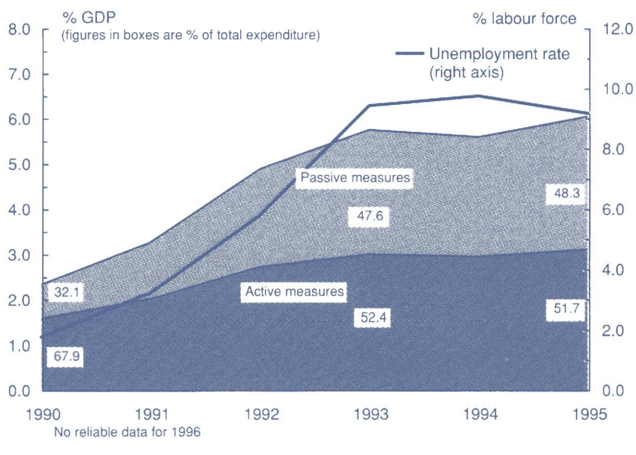
57 France, 1990-95



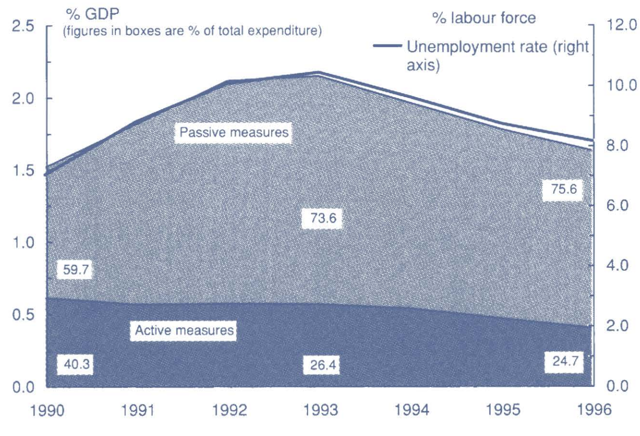
58 Germany, 1990-96



59 Sweden, 1990-95



60 UK, 1990-96



61 Spain, 1990-96

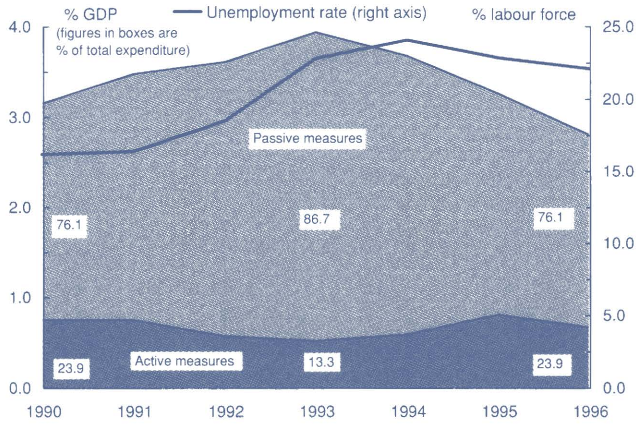


Table 8 — Expenditure on active and passive labour market measures, 1985–96

	B	DK	D	GR	E	F	IRL	L	NL	O	P	SF	S	UK	E14
1985															
Total expenditure	4.7	5.1	2.4	0.5	3.2	3.1	5.0	1.5	4.7	1.2	0.8	2.3	3.0	2.8	2.9
Active measures	1.3	1.2	0.8	0.2	0.3	0.7	1.5	0.5	1.3	0.3	0.4	0.9	2.2	0.7	0.8
Passive measures	3.4	3.9	1.4	0.4	2.9	2.4	3.5	1.0	3.4	0.9	0.4	1.3	0.9	2.1	2.1
of which: early retirement	0.9	1.2	0.0	0.0	0.0	1.2	0.0	0.7	0.0	0.1	0.0	0.5	0.1	0.1	0.4
1990															
Total expenditure	3.8	5.7	2.1	0.8	3.2	2.7	4.1	0.9	3.9	1.3	1.0	2.2	2.4	1.5	2.4
Active measures	1.2	1.3	1.0	0.4	0.8	0.8	1.4	0.3	1.2	0.3	0.6	1.0	1.6	0.6	0.9
Passive measures	2.6	4.4	1.1	0.5	2.4	1.9	2.7	0.6	2.6	1.0	0.4	1.1	0.8	0.9	1.5
of which: early retirement	0.7	1.2	0.0	0.0	0.0	0.6	0.1	0.5	0.0	0.1	0.1	0.5	0.1	0.0	0.2
1993															
Total expenditure	4.2	7.5	4.2	0.7	4.0	3.4	4.5	0.9	4.4	1.8	1.8	6.7	5.8	2.2	3.7
Active measures	1.2	2.0	1.6	0.3	0.5	1.3	1.6	0.2	1.4	0.3	0.9	1.7	3.0	0.6	1.2
Passive measures	3.0	5.5	2.6	0.4	3.4	2.1	2.9	0.7	3.0	1.4	0.9	5.0	2.8	1.6	2.4
of which: early retirement	0.7	1.4	0.6	0.0	0.0	0.4	0.2	0.4	0.0	0.1	0.1	0.5	0.1	0.0	0.3
1996															
Total expenditure	4.2	6.6	3.8	0.8	2.8	3.1	4.1	0.9	4.7	1.8	2.1	5.4	6.1	1.6	3.4
Active measures	1.4	2.3	1.4	0.3	0.7	1.3	1.7	0.3	1.4	0.4	1.1	1.7	3.2	0.4	1.2
Passive measures	2.8	4.3	2.4	0.4	2.1	1.8	2.4	0.7	3.4	1.4	1.0	3.7	3.0	1.2	2.2
of which: early retirement	0.7	1.8	0.0	0.0	0.0	0.4	0.1	0.3	0.0	0.1	0.1	0.4	0.0	0.0	0.2

Note: DK, P 1985=1986, IRL 1993=1994, B, GR, F, S 1996=1995, I data not available

markedly over the 1990s, though the fall was largely concentrated in the early years of the period when unemployment went up sharply in all four countries. Indeed, since unemployment has stabilised, as it has in most countries since 1993 or 1994, spending on active measures has risen relative to that on passive measures in a number of Member States, most especially in Belgium, Luxembourg, Finland and Spain, in the last of which the share almost doubled (Graph 61).

In general, therefore, there is some evidence that expenditure on passive measures of income support was successfully reduced in the period 1993 to 1996 in most Member States after the recession came to an end and unemployment stabilised, in line with Government policy aims across the Union, and that the share of spending devoted to active measures has risen in a number of countries, even if only slightly.

The commitment made by Member States at the Luxembourg Job Summit to increasing employment and improving the employability of the work force should lead to a more marked shift towards active measures in the future.

Chapter 5 Reforming the transition from work to retirement

For many years, there has been a significant upward trend in most parts of the Union in the number of people retiring from work before reaching the official age of retirement. During the latter part of the 1970s and over the 1980s, in particular, as unemployment increased and remained high, early retirement was either actively encouraged or tacitly accepted in order to reduce both the registered figures and the number actually looking for jobs. In more recent years, the prevailing attitude has changed, in response partly to the growing cost of early retirement schemes, partly to the large increase in the number of people above the official retirement age and the relative decline in working-age population which is set to occur in 10–15 years time in all Member States (see Chapter 1 above).

Policy attention across the Union has, therefore, focused on modifying social protection systems to deter rather than encourage early retirement. As part of this, consideration is being given not just to the removal of measures which provide income support to those retiring early but also to more imaginative schemes of partial retirement, which achieve the aim of reducing costs but which, at the same time, help the people concerned make the transition to full retirement, while enabling employers to benefit from their experience and expertise for longer. At the same time, from the employers' perspective, partial retirement can be seen, not as an alternative to early retirement, but as a means of having the government pay part of the costs of keeping people in work until they reach official retirement age.

The concern here is to examine the changes which have occurred in government policy across the Union towards retirement in recent years, the objectives which they have been aimed at achieving and their effects so far. The focus, in particular, is on the more innovative schemes which have been introduced to encourage people to remain in work longer on a part-time basis. First, however, the trend towards early retirement in different Member States is examined in some detail on the basis of data from the Community Labour Force Survey, which are also used to throw light on the relative number of people nearing retirement age working part-time and the extent to which this has changed in recent years.

The growth of early retirement

In most Member States, the official age of retirement is 65 for men — with only a few exceptions, such as France where it is 60 and Denmark where it is 67 — and, with more exceptions (Germany, Portugal and the UK, for example, where it is 60), the same for women. The effective age of retirement is, however, significantly below this in all Member States. In no country in the Union are more than half of men aged 60 to 64 still in employment and in every country apart from Sweden, fewer than 30% of women in this age group are still working. The effective age of retirement for men, moreover, has come down throughout the Union over the past decade. For women, there has been comparatively little change in general, though the strong upward trend in the participation of women in the work force, which is evident for younger age groups, serves to conceal any tendency for the increasing number in work to retire early.

Men

The growth of early retirement among men is most evident for those aged 55 to 64. For the younger age group, 50 to 54, though there has been some rise in the proportion who are 'permanently' economically inactive (the measure chosen of those who have retired — see Box), it was relatively small between 1986 and

Data on early retirement

The Community Labour Force Survey is the main comparable source of data on early retirement in Member States. Identifying the number of people who have retired before they reach the official age from this, however, is not straight-forward. While the LFS gives details of the employment status of men and women by age group, including of those who report themselves as being economically inactive because they are retired, not all people who have effectively stopped working will be included in this category. Others who class themselves as being inactive because of disabilities or for other reason may equally be retired in practice (especially since in some Member States disability benefits have been used as a means of providing income support to those who are unable to find a job and are close to retirement age). Equally, some of those classed as unemployed in the older age groups will never work again, especially those who have been out of work for a long time.

The data used here to indicate trends in early retirement relate to those in the older age groups who are wholly and permanently economically inactive for whatever reason, so that they include those with disabilities, for example, but exclude those on short-term layoff or temporarily ill. They also exclude those classed as unemployed. Though, as noted, many of these in the age groups concerned may never return to work, they should, nevertheless, still be actively looking for a job, otherwise under the ILO convention adopted by the LFS, they ought not to be classified in this category. Accordingly, they cannot be regarded as retired in the true sense of the word. Although this argument should not be pushed too far, because it may well be that many of the long-term unemployed, in particular, are not really actively involved in job search, in practice the number unemployed in the older age groups tends to be comparatively small and, with a few exceptions (Germany being the main one), has not changed much over the past decade or so. The results of the analysis, therefore, would not be greatly altered if the unemployed were counted as being retired, though it would add a few percentage points to the proportion no longer in the work force.

These arguments relate largely to men. For women, it is still the case over much of the Union that comparatively few in the older age groups have pursued working careers so that a high proportion of them were economically inactive even when they were younger.

1996 and, in the Union as a whole, only some 12% fell into this category in the latter year (Graph 62). There are, however, some exceptions. In particular, in Belgium and Finland, the proportion was over 17% in 1996 — though in the former, it has fallen from over 20% in 1990 — and in Italy, it was just over 20%, the only country to show a marked upward trend over the past decade, apart from the UK. Nevertheless, in most Member States, the proportion who are economically inactive is not much higher than for younger age groups.

For men aged 55 to 59, by contrast, the proportion still in the work force is much lower throughout the Union and in most countries there has been a significant increase over the past decade in those who are retired. In the Union as a whole, some 30% of men in this age group were economically inactive in 1996, in most cases, well before they had reached the official retirement age. In Italy (where the official age for men was 62) and Finland, just over 40% were no longer in the work force, in Luxembourg, over 45% and in Belgium (where men could retire from 60 on), 50% (Graph 63). Only in Denmark, Germany and, above all, Sweden, was the proportion below 25%.

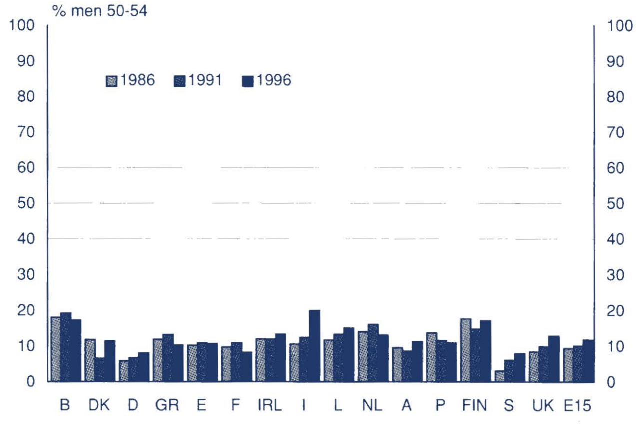
Over the 10 years, 1986 to 1996, the proportion not in the labour force increased in all Member States, except Finland, though the rise was small in Greece, France and Portugal, and in Luxembourg and Austria (though there is some doubt about the consistency of the data in the latter because of the lack of an LFS for earlier years) as well as Greece, the proportion declined between 1990 and 1996. The increase was especially marked, as for the 50–54 age groups, in Italy and the UK (where the proportion rose by almost 10 percentage points and by almost 7 percentage points respectively).

Of men aged between 60 to 64, two-thirds were no longer in the work force in the Union in 1996, over 75% in Finland, almost 80% in the Netherlands, over 80% in Belgium and Luxembourg and almost 90% in France (Graph 64). While the high figure in France might be expected because the official age of retirement is 60, in all the other countries listed, with the partial exception of Belgium, where it is possible for men to retire any time between 60 and 65, the official retirement age is set at 65. In only three Member States, Ireland, Portugal and Sweden, were more than half of men in this age group either still working or actively seeking work.

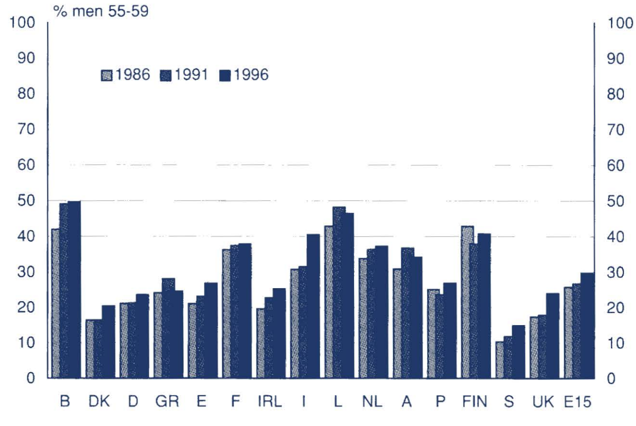
In all countries, apart from Luxembourg and Austria, the proportion of men aged 60 to 64 who were no longer in the labour force increased between 1986 and 1996 and in all of these, except Greece and Belgium, there was a rise during the 1990s. In this case, the largest increases (all over 10 percentage points) occurred in Denmark, Spain, France and Ireland.

From the above, for both the 55 to 59 and 60 to 64 age groups, the increase in the relative number of men no longer economically active appears to have been greater during the 1990s than over the latter part of the 1980s — in other words, over the period when policy towards early retirement, as documented below, had supposedly been reversed towards discouraging rather than encoura-

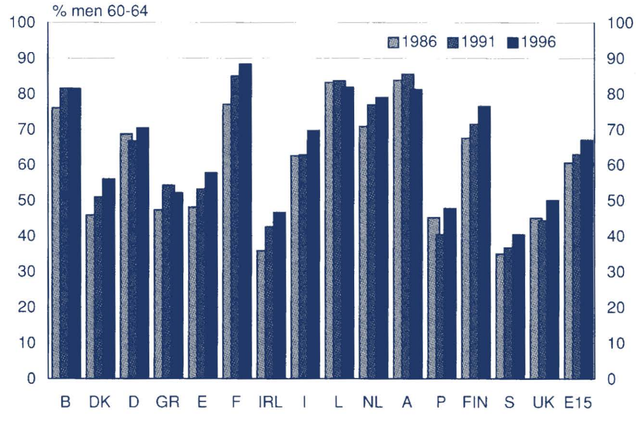
62 **Inactivity rates of men, aged 50-54, in Member States, 1986, 1991 and 1996**



63 **Inactivity rates of men, aged 55-59, in Member States, 1986, 1991 and 1996**



64 **Inactivity rates of men, aged 60-64, in Member States, 1986, 1991 and 1996**



ging men to stop work before they reached the official retirement age. This observation, however, needs to be qualified. The changes which have occurred over the past decade reflect the influence not only of policy but, arguably even more, of changes in underlying economic circumstances. Between 1986 and 1991, there was a general upturn in the European economies, accompanied by an unprecedented rate of employment growth. In a number of Member States, the proportion of men aged between 55 and 64 no longer in the work force, especially towards the younger end of the age group, declined or remained much the same rather than increased. After 1991, the European economies went into recession, depressing employment growth, and inactivity rates rose in nearly all countries.

Moreover, examining the changes which occurred between 1991 and 1996 in more detail reveals that much of the rise in economic inactivity took place in the earlier years of recession between 1991 and 1994 and since then the increase has slowed down. Nevertheless, over the two years, 1994 to 1996, the proportion of men aged 55 to 59 no longer in the work force fell in only five Member States (Greece, France, Ireland, the Netherlands and Austria) and then only marginally. Similarly, the proportion for those aged 60 to 64 also fell in only five cases — the three Nordic countries together with Greece and Germany — again only slightly in the last two, but more significantly in the other three following a large rise in the recession years.

In addition, though the rise in early retirement may have slowed down since 1994, coinciding with the shift of emphasis in government policy across the Union, on the experience of the 1980s, some slowdown would be expected after the recession came to an end and job shortages became less acute. It remains to be seen whether the recent slowdown signifies an end to the upward trend and whether the policy change will prove effective, not just in slowing the increase in the number of people retiring early, but in reversing it.

Women

In the case of women, as noted above, any trend towards early retirement has been concealed by the marked tendency for increasing numbers to pursue working careers right across the Union. Accordingly, a trend is apparent only among women close to the official age of retirement. (In practice, the data on changes over time in labour force participation among older women reflect the effect, in large measure, of younger age groups with higher participation levels becoming older — the so-called cohort effect — rather than of more women deciding to enter the work force at a comparatively old age.) For those aged 50 to 54, the rate of participation of women in the labour force went up markedly from around 40% in 1986 to 50% in 1996 in the Union as a whole, the rate increasing in all Member States, except Greece, where participation remained low, and Denmark and Sweden, where it fell from a high level (75% in the former and almost 90% in the latter) (Graph 65).

For women aged 55 to 59, labour force participation also rose over the 10 years 1986 to 1996 in most Member States but less markedly. The proportion of those wholly inactive in the Union declined from 65% to 58% over the period, with only Denmark, Greece (as for the 50 to 54 age group) and Luxembourg showing an increase, though the fall in Italy, Austria, Sweden and the UK was only small (Graph 66). The fall in the proportion was particularly large (over 10 percentage points) in Germany and the Netherlands, in both cases concentrated in the 1990s.

These changes have had some effect in reducing the difference between Member States in the relative number of women in this age group who are permanently economically inactive. Nevertheless, this remains extremely wide, ranging from over 85% in Luxembourg and just under 80% in Belgium and Italy to around 45% in Denmark, Finland and the UK and only 20% in Sweden.

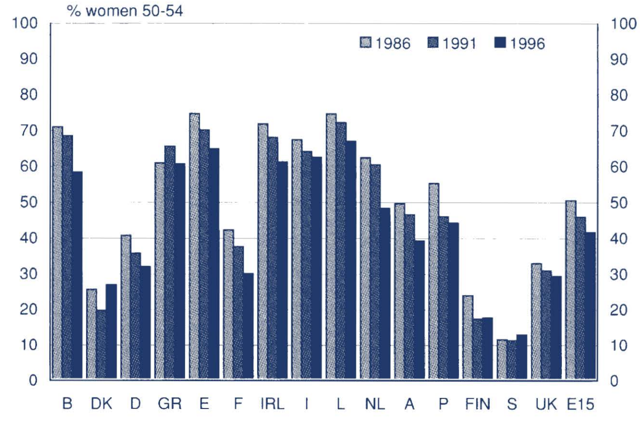
For women aged 60 to 64, there was virtually no change at the Union level between 1986 and 1996 in the proportion who were economically inactive, the upward trend in participation being cancelled out by the trend towards early retirement. Only three Member States, Portugal, Sweden and the UK, showed a significant reduction (over 5 percentage points) over the 10 years, with Denmark, Luxembourg and Finland showing even larger increases (Graph 67). Moreover, in the former three countries, almost all of the fall occurred in the first five years of the period, with virtually no change between 1991 and 1996. Indeed, only in Denmark and Luxembourg, where it rose, and in Greece, Ireland and Austria, where it fell, was there more than a marginal change in the proportion who were inactive during the 1990s.

Differences between Member States in the relative number of women who are inactive are much narrower for this age group than for the younger one, with the proportion in 5 countries being over 90% and 80% or higher in 7 others, only the UK (75%), Portugal (70%) and Sweden (only 45%) having a figure less than this. The great majority of women aged 60 to 64, therefore, are not in the labour force in the Union. Nor does it seem that the official age of retirement has much effect on this. In the UK, for example, the official age is 60 and in Portugal, 62, lower than in most other Member States where it is 65, yet the relative number of women still in the work force is higher than in all other countries, apart from Sweden. In the light of this, it is open to question how far the present policy in a number of Member States, including Portugal and the UK, of increasing the official retirement age of women will reduce the number in their early 60s no longer in the work force.

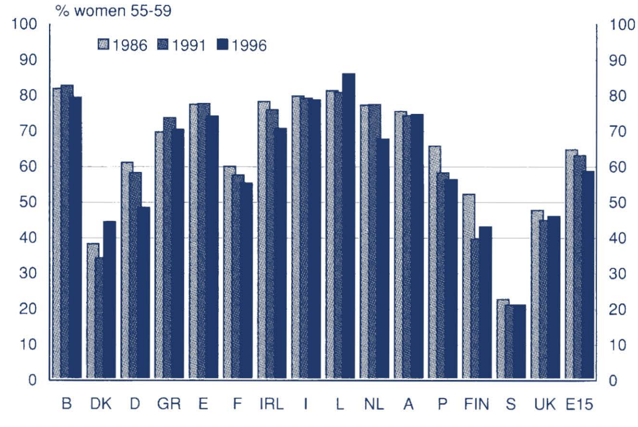
Reasons for inactivity

Data from the Community Labour Force Survey throw some light on the reasons for early withdrawal from the work force across the Union, which, in turn, seem to reflect some differences in the approach to providing income support to the people concerned in different Member States. Whereas most of the men aged 60 to 64 in the Union who were no longer economically active in 1996 classed themselves as being retired, significant proportions in a number of

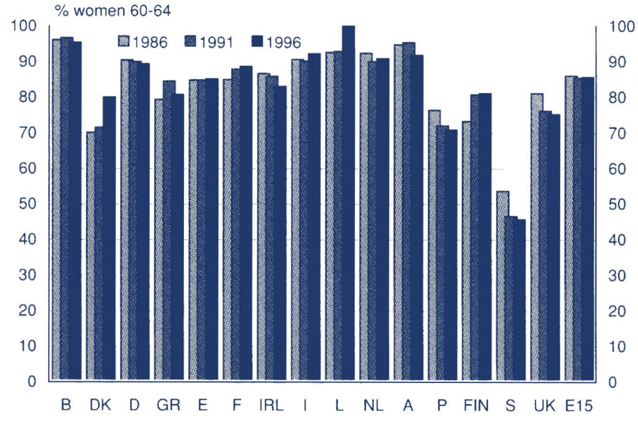
65 Inactivity rates of women, aged 50-54, in Member States, 1986, 1991 and 1996



66 Inactivity rates of women, aged 55-59, in Member States, 1986, 1991 and 1996



67 Inactivity rates of women, aged 60-64, in Member States, 1986, 1991 and 1996



countries gave other reasons for no longer being in the work force, especially being disabled. Indeed, in the UK, more men in this age group not in the work force classified themselves as disabled than as retired, some 25% of all men aged 60 to 64, the same proportion as in Finland and only slightly more than in the Netherlands (20%), though in both the latter countries, the relative number of men classed as retired was much greater (Graph 68). By contrast, in Greece and Italy, under 5% of men of this age classed themselves as disabled (in France, Austria, Portugal and Sweden, this was not even included as an option in the survey).

Much the same pattern of differences is evident for the 55 to 59 age group. In the UK, again most of the men not in the work force classed themselves as disabled and very few as retired, in Finland and Denmark, more were also classified as disabled than retired and in the Netherlands and Ireland, the numbers were similar, while in Greece and Italy, there were very few men not working because of disabilities.

For the 50–54 age group, there were smaller differences between countries in the relative importance of disability as a cause of inactivity, excluding those where the option was not included in the survey. It was, nevertheless, much greater in the UK, Finland and the Netherlands than in Germany, Greece, Spain and Italy.

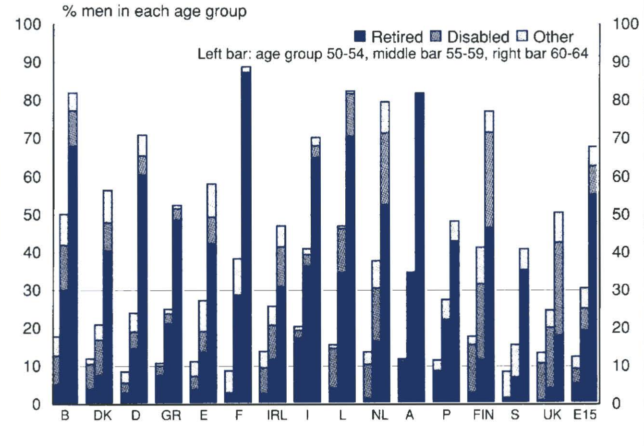
It is difficult to believe that these differences reflect actual variations in the incidence of disability across the Union, rather than the differential use of disability benefits as a means of providing income support for men no longer in the work force.

For women, the proportion classing themselves as retired was relatively small for those in their 50s in most Member States, exceeding 20% of the 55 to 59 age group only in Italy, Austria and Portugal and being less than 5% in Spain, Ireland and the Netherlands, all countries where the proportion of women of this age not working was higher than the Union average (Graph 69). The figures for economic inactivity reported above, therefore, may be poor indicators of the extent of early retirement among women, though in the UK, Finland and Denmark, the number of women not working because of disability, some of whom might effectively be retired, is relatively high, as in the case of men.

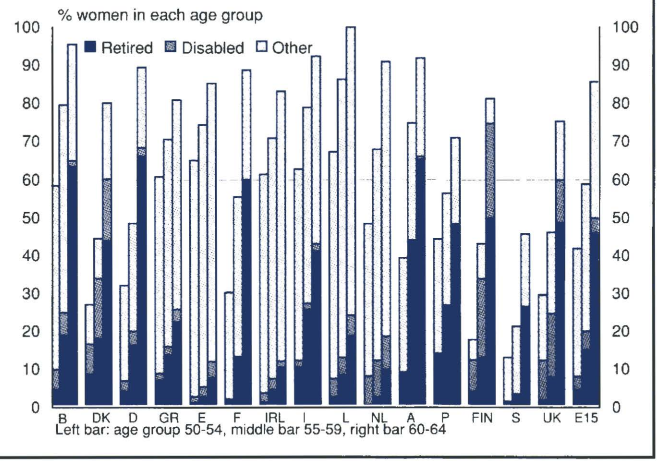
Policies to reduce early retirement

The greatest efforts in recent years to reduce the extent of early retirement and encourage people to remain longer in work have been made in Member States where rates of economic inactivity among men in their late 50s and early 60s have risen to high levels. Indeed, measures have been introduced to change pension systems in all 9 countries with the highest inactivity rates for men in this age group, as indicated above. It should be recognised, however, that a major aim of these policies is to reduce the cost falling on systems of social protection, independently of their effect on early re-

68 Inactivity rates of men by age group in Member States, 1996



69 Inactivity rates of women by age group in Member States, 1996



tirement *per se*. These measures are described below.

Increases in the retirement age

All governments in the above countries have increased the official age of retirement and/or extended the contribution period required for a full pension. In Germany, the retirement age will be progressively increased to 65 for both men and women between 2001 and 2012, even in the case of men, for those who have paid contributions for 35 years or more who at present are able to retire once they reach 63. From 2002, if they retire they will suffer a reduction of 18% in pension. Equally, the retirement age has also been increased for the unemployed, who at present can draw a full pension at 60 if they have received unemployment benefit for at least 52 weeks. Though they will be allowed to retire up to three years earlier, they will also have their benefit reduced if they do so (by 3.6% a year).

In France, while the age of retirement has not been increased since it was fixed at 60 in 1982, from 1994, the period of contributions required to qualify for a full pension was raised progressively from $37^1/_2$ to 40 years (6 additional months being added each year). This was coupled with a change in the reference salary for calculating the pension payable, from the average of the last 10 years of a person's working careers to the average of the best 25 (one year being added each year up until 2008).

In Italy, the pension system is perhaps the one which most encourages early retirement in Europe, in that workers can retire after 35 years of work once they have reached 52, or if they have accumulated 36 years of contributions irrespective of their age. For civil servants, the requirements are even less stringent. Though the new system being phased in following the 1995 pension reform will continue to allow both men and women to retire any time between 57 and 65, the pension payable will be based more on contributions paid and less on previous salary. The transition period, however, is extremely lengthy, extending to 2030, and will involve a substantial financial deficit, which may prove difficult to sustain. (At the end of 1997, the government and unions agreed to a small reduction in the transition period and faster convergence of the rules for the various present schemes, in line with the recommendations of the Onofri Report.)

In Spain, the Toledo Pact (of February 1995) attempted to improve the financial viability of the pension system by increasing the age at which people retire. It recommended that early retirement should be penalised and that the Government should encourage people to remain in work longer through reductions in social contributions. (Legislation was passed in July 1997 to rationalise the social protection system and to implement many of the recommendations of the Toledo Pact, though it remains to be seen how effective this will be. It might also be noted that according to a survey carried out in 1995, a large majority of Spaniards were against raising the retirement age but in favour of more flexible arrangements under which partial retirement could be combined with part-time employment.)

In Belgium, the retirement age of women is being increased progressively from 60 to 65, the same as for men, by 2009, and the number of years of contributions necessary to qualify for a pension is being raised gradually from 20 to 35 beginning in 1997 (the process being completed by 2005). In addition, social contributions on early retirement pensions have been raised from 4.5% to 6.5%. In Finland, the Pension Committee in 1990 set the objective of raising the official age of retirement from 65 to 68 by the year 2020 and a number of amendments to the pension system were introduced in 1994 to deter early retirement, including increasing pensions for those continuing to work after 60, raising the qualifying age for early retirement from 55 to 58 and reducing that for partial retirement from 60 to 58 and increasing the official retirement age for public sector workers from 63 to 65.

In Austria, as noted above, the actual age of retirement is well below the official age (60 for women, 65 for men) and since 1996, a number of measures have been introduced to contain costs. In particular, the period of contributions has been increased from 35 to $37^1/_2$ years (which is likely to affect women more than men), while for those retiring early because of being unemployed, it was increased from 15 to 20 years in the last 30. In addition, the formula determining the amount of pension receivable was modified giving an additional disincentive to retire early (specifically, the percentage applied to earnings for the first 30 years of employment was reduced slightly and that applied to the following 15 years increased, so reducing the amount for those retiring before completing 45 years). In the Netherlands, where the effective age at which people retire is also one of the lowest in Europe, however, the emphasis of policy reform has been more on combating discrimination against older workers in the labour market.

From early retirement to partial retirement

The second set of policy measures has been aimed at reducing outflows of older workers from the labour market, both by limiting the number who qualify for early retirement and by encouraging, and making it possible for, those approaching retirement age to work part-time rather than to stop work completely. In a context where job shortages remain a major problem, the latter type of arrangement is, in some sense, a compromise between combating unemployment and keeping older workers in employment and, indeed, in a number of countries has included an obligation for companies to take on other people at the same time.

In Belgium, flexible retirement between 60 and 65 has been possible for all male employees since 1990 (and will be possible for women once their retirement age has been increased to 65), the pension payable varying according to the employment record of the person concerned. A total or partial career break scheme has been in place since 1985, entitling employees aged 50 to opt for part-time work for a maximum of three years, until they reach the age of 60, when they are able to retire. The number doing so, however, is limited to 1% of the work force and companies are required to take on new employees to replace those opting for part-time work. A new measure, introduced in 1993, enables people to continue working part-time once they reach 55, those concerned receiving an allowance paid partly from the unemployment insurance fund and partly by employers on top of their wage, employers being obliged to offer a job to someone unemployed at the same time. These measures, however, have not had a perceptible effect on the number of older workers in employment, as indicated above, and, by September 1997, only a few hundred people had opted for part-time early retirement.

In Austria, qualifying conditions for early retirement have also been tightened, while gradual retirement has been encouraged by the introduction, in 1993, of a partial early pension scheme, under which women aged 55 to 60 and men of 60 to 65 can reduce their hours of work by 50% and receive 70% of the full pension or by 70% and receive 50% of the pension. Although the option appears financially attractive, in practice, almost nobody has taken advantage of the option, possibly because those eligible also qualify for full early retirement and a full rather than partial pension.

In Finland, partial pension schemes were introduced at the end of 1980s with the intention of smoothing the transition to retirement and reducing the number retiring early. According to recent studies, however, such schemes are more an alternative to full-time work than to full-time retirement and have reduced the number of full time workers rather than of pensioners. Two other measures, *Part-time Work Supplementary Benefits* and *Job Rotation Compensation*, have been subsequently introduced to reduce hours of work. Both are payable to those working full-time for the same employer for at least a year and require that the employer take on someone unemployed to compensate, though so far they seem to have had little effect.

In Germany, as well as the criteria for eligibility for early retirement being tightened, a partial retirement scheme was introduced in 1996 for a limited period of 5 years, enabling those over 55 to work part-time, the reduction in their income being compensated from the unemployment insurance fund (30% for a 50% reduction in working time). As elsewhere, employers are required to take on either people unemployed or trainees to fill the part-time jobs so created. So far, however, the number of such jobs has been relatively small.

In Denmark, a partial retirement scheme (*Early Partial Retirement Pay*) was introduced in January 1995, with the same conditions applying as for full early retirement and open to people in the same age group, 60 to 67. By September 1996, just under 900 people had opted for this scheme.

In Italy, it has been possible since October 1996 for employees eligible for a seniority pension to work part-time, enabling a job to be created for someone younger, though, in practice, the option has not been much exploited, while in Spain, the Pact of Toledo included a reference to the case for introducing measures to facilitate flexible retirement, but so far no action has been taken.

In France, partial retirement has probably been more developed during the 1990s than in any other Union country, in an attempt to reduce the scale of early retirement and the costs involved, as well as keeping older workers in employment and so maintaining the payment of social contributions. Measures to encourage employers to keep on older workers date back to 1985 when they were introduced to enable employees over 55 to work part-time, the reduced wage being topped up by an allowance (of 20–30% of previous salary) from the Unemployment Insurance Fund and employers being required to take on new workers for the part-time jobs so created. The scheme was amended in 1992, giving employers the option of paying a financial contribution instead of hiring new workers — so catering for declining firms for which part-time working was a means of avoiding redundancies — and easing the constraint on them to take on those in priority groups (to a third of, for example, young people under 26 with low educational qualifications, people with disabilities, unemployed over 50 and/or the long-term unemployed).

The scheme was further relaxed in 1994, under the 5-year Employment Act, enabling the reduction in hours of work to be varied between 20% and 80% of annual full-time hours worked in the preceding year, so long as it averages 50% over the whole gradual retirement period. In 1995, the number opting for gradual retirement increased by 20% after doubling the year before and, for the first time, exceeded the number opting for full early retirement.

In the Netherlands, the 'older workers' directive', which allowed firms to dismiss older workers first in the event of redundancies, was abolished in 1994. In addition, measures were introduced to limit access to the three early retirement schemes: disability, for long the main pathway into early retirement, unemployment and the *VUT* (voluntary pre-retirement) scheme, the latter originating from a collective agreement between employers and employees and financed mostly by business. This contrasts with the other schemes which are funded partly by the beneficiaries themselves, which is likely to discourage them from opting for early retirement and is a reason why the Government is trying to encourage a shift from *VUT* towards these.

As noted in Chapters 2 and 4, the disability benefit system has been tightened considerably in recent years, those claiming benefit now needing to satisfy more stringent medical examinations of their ability to work. At the same time, responsibility for funding has been shifted more on to employers whose contribution rates vary partly according to the number of claimants they employ (see Chapter 4).

The criteria determining entitlement to disability benefits have also been tightened in the UK, where they have also been used in the past to support effective early retirement, while in Sweden — where, like the UK, withdrawal of workers from the labour market is less of a feature than in the rest of the Union — receipt of an early retirement pension now depends on establishing incapacity for work.

In Sweden also, the minimum age for entitlement to partial pension was raised from 60 to 61 in 1994, accompanied by a reduction in the rate of pension from 65% of previous earnings to 55% and a limitation on the maximum reduction in working hours of 25%. These changes have led to a significant fall in the number of people opting for a partial pension.

Keeping older workers in employment

The third aspect of policy has been to encourage businesses to retain older employees in work.

Increases in the official age of retirement are likely to have very little effect in this regard if they are not accompanied by measures to protect older workers. Government policies, however, have not changed significantly over the past few years in this area and have generally not been very successful in persuading employers to change their policy in this respect. In Germany, in particular, long-term unemployment has risen significantly among older workers since unification and, unlike in other Member States, the rate for these is higher than for their younger counterparts.

Nevertheless, under employment promotion legislation, older workers are treated as a priority group and a number of measures exist to encourage their employment, the most important of which are age-dependent wage subsidies offered to firms recruiting those of 50 or over and who have been unemployed for at least 18 months to part-time jobs. This, however, as noted, does not seem to have had much effect in increasing the number of older workers taken on, though it is always difficult to know what would have happened in the absence of the measure. A possible unfortunate effect of this kind of targeting, which is often difficult to avoid, is to reinforce prejudices against employing the group in question simply because they are targeted which is liable to give the impression that they are somehow inferior workers.

In France, active labour market policies in favour of older workers were introduced at the end of the 1980s, as part of a programme to combat long-term unemployment. As in Germany, these were aimed at encouraging businesses to take on those over 50 who were unemployed, taking the form of wage subsides and exemptions from social contributions. They were replaced, in 1995, by a new measure in a similar but slightly more extended form (*contrat initiative emploi*), which has mainly benefited those under 45 rather than those over 50.

Other measures, however, have also been introduced, including one requiring employers to pay additional contributions if they dismiss anyone over 50 and, perhaps most importantly, another, implemented in 1994, encouraging them to continue to train older workers and to enable them to participate in company training programmes so that they can extend and improve their skills and qualifications. A further measure, moreover, concerned with increasing working-time flexibility, enables workers to accumulate entitlement to paid leave, which *inter alia* gives businesses a greater opportunity to manage leave for older workers nearing retirement.

Nevertheless, so far, as in Germany, these various measures have not proved very effective in keeping older workers in employment.

In Finland, there seems to be a greater commitment than in most other parts of the Union to establishing an integrated programme of active measures for those over 45. Since 1990, the measures implemented include:

- the *FinnAge* programme established in the Finnish Institute of Occupational Health to promote the health, employability and well-being of those over 45 which involves research and other activities in firms, training organisations and expert services;
- the *Small Workplace* programme, a cooperation programme of the Finnish Institute of Occupational Health with small firms, aimed at encouraging them to adopt best practices in the interests of the welfare of their employees as well as themselves;
- the *Employability for Tomorrow* programme, implemented by the Federation of Employment Pensions Institutes, aimed at fostering education and the dissemination of information to improve the employability of older workers;
- the *National Programme for Older Workers*, launched by the Government at the beginning of 1997 for a 5-year period for improving the job opportunities open to older workers and consisting of changes in legislation, the provision of information, training and research and the general promotion of activities to help older workers improve their skills.

At the same time, these active measures co-exist with passive ones which provide income support to older workers losing their job, in the form of unemployment allowances or pensions payable until the official age of retirement as well as disability benefits, which are the most common means of supporting those who effectively retire early. Nevertheless, the various programmes listed above seem to have reduced the number claiming the latter benefit in the recent past, though it remains high as compared with other Member States (see Chapter 4).

Other measures

In all the Member States cited above, the possibility exists for people to opt for partial retirement in the later stages of their working careers. In some countries, however, pension regulations make this difficult. In the UK, for example, where early retirement *per se* has so far been less of an issue — though it has surfaced in the form of growing concern about the number of people drawing disability benefit — the rules governing occupational pensions prohibit someone receiving a pension to continue to work part-time for the same employer as before. The development of partial retirement, therefore, requires the removal of obstacles as well as the implementation of positive measures.

There is also a potentially important role for information and anti-discrimination measures, which draw attention to the advantages of hiring or continuing to employ older workers and which discourage employers from regarding age as an issue in recruitment policy.

Older men employed part-time

It remains to examine the relative scale of part-time working across the Union and whether it has tended to increase in recent years in response to the measures listed above, though since in a number of cases these have been introduced only very recently, any effect may not as yet be evident. Nevertheless, even in these cases, the prevailing level relative to that in other Member States as well as past changes are relevant to an assessment of their possible effect in future.

Only a comparatively small number of men in the Union work part-time, though the proportion has risen significantly over the 1990s. In the 25 to 49 age group, which is the relevant basis for comparison, just under 3½% of men employed in the Union worked in part-time jobs in 1996, and only in the Netherlands (9½%), was the proportion over 5%. For men aged 50 to 54, the proportion working part-time is much the same as for the younger age group in all Member States — the biggest difference being in the UK, where it is 1½ percentage points higher, and Denmark, where it is lower by a similar amount.

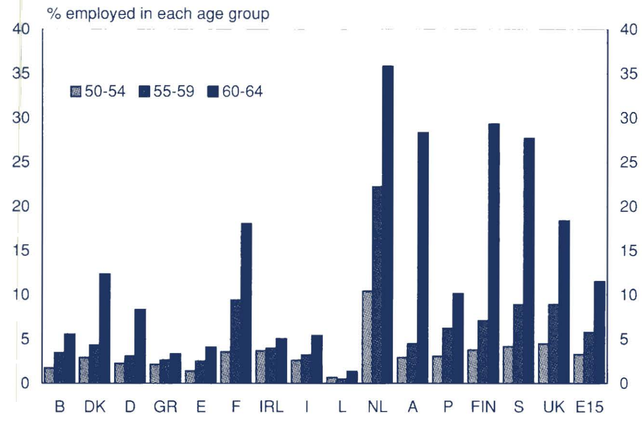
For men aged 55 to 59, the relative number of those employed working part-time is generally higher, but only to a comparatively small extent in most cases. In the Union as a whole, just over 5½% of men in this age group were employed in part-time jobs in 1996 as against just under 3½% for those aged 50 to 54, and in 9 of the 15 Member States, the difference was less than 2 percentage points (Graph 70). The 6 countries where it was greater are the Netherlands (where the share working part-time in the older age group was almost 10 percentage points higher than in the younger group), France (6 points higher), Sweden and the UK (4½ points higher) and Portugal and Finland (3 points higher). Of these, only France and Finland had partial retirement schemes in operation, though in the Netherlands, much more than in any other country, policy generally is to encourage part-time working. In the other three countries, it is perhaps relevant that the extent of labour force participation of men aged 55 to 59 is among the highest in the Union, which may owe something to the relative importance of part-time working.

Among men aged 60 to 64, the proportion of those in employment working part-time in the Union is over twice that for the 55 to 59 age group, but was still under 12% in 1996. While in all Member States, the proportion was higher than for the younger age group, the difference was small (2 percentage points or less) in Greece, Spain, Ireland, Italy, Belgium and Luxembourg, in all of which men of between 60 and 64 working part-time accounted for 5½% or less of all those in employment. Nevertheless, in the first three of these countries, a higher proportion of men in this age group remain in the work force than in the Union as a whole. In the latter two, by contrast, the proportion is among the lowest in the Union. In Belgium, measures have been introduced to increase partial retirement, as they have also been in Italy, though too recently to affect the position in 1996.

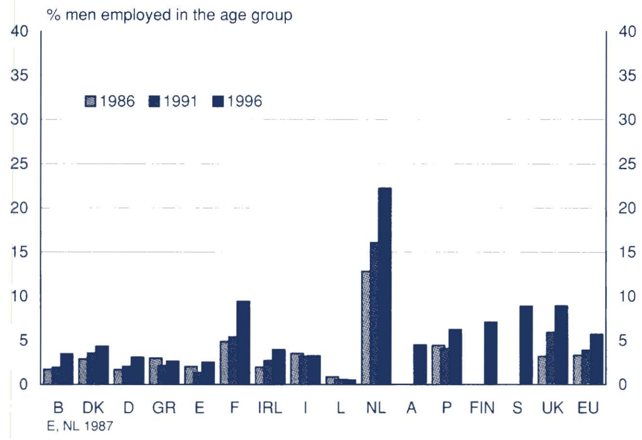
Of the remaining countries, in four — the Netherlands, Austria, Finland and Sweden — the proportion working part-time in 1996 was over 25% of men in this age group in employment. In the first three, labour force participation was below average, in the fourth, Sweden, the highest in the Union. In addition, in two of the countries, measures are in force to encourage part-time working among employees approaching retirement age, in two not. There is, therefore, little sign of any relationship between the importance of part-time working and either labour force participation among older workers or measures operating to increase this.

For men of 65 and over, part-time working is much more important, around 40% of all those in employment being in part-time jobs. The number of this age still in work, however, is very small — only some 6% of the 65 to 69 age group in the Union in 1996. Moreover, in countries where the latter proportion was relatively high — Greece (14%), Ireland (15%) and Portugal (24%) — the relative number working part-time was below rather than above average, though this in some degree reflects the high proportion of men in this age group employed in agriculture.

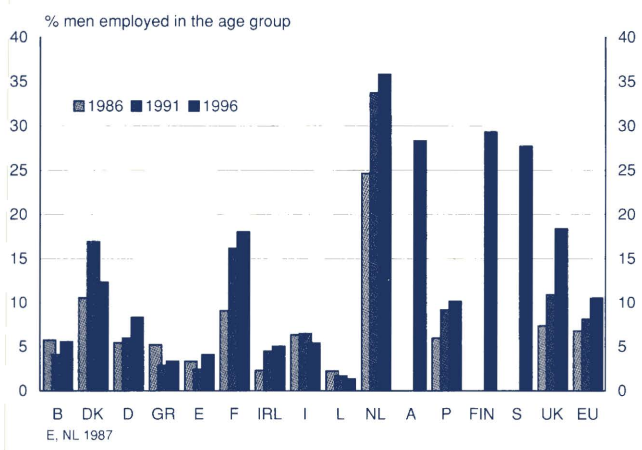
70 Men employed part-time by age group, 1996



71 Part-time working of men aged 55-59, 1986, 1991 and 1996



72 Part-time working of men aged 60-64, 1986, 1991 and 1996



Changes in part-time working of men

As noted above, the relative number of men working part-time has risen significantly over the 1990s, and this has been true even more for older workers than their younger counterparts. For men aged 50 to 54, the proportion in work employed part-time in the Union increased from 2% in 1991, the same as in 1986, to just over 3% in 1996. A similar increase occurred for those aged 25 to 49.

For men aged 55 to 59, the proportion in part-time jobs rose from just under 4% in 1991 to just over $5^1/_2$% in 1996, with all Member States except Italy and Luxembourg recording an increase (Graph 71). The rise exceeded 4 percentage points in France and 6 percentage points in the Netherlands, both countries in which measures have been taken to increase the numbers opting for partial retirement, though in the latter, as part of a more general policy of encouraging part-time working. Over the 10 years 1986 to 1996 as a whole, however, the rise in France was slightly less than in the UK, where there were no special measures for encouraging part-time working, though the almost complete absence of restrictions enabled part-time working to develop.

For men aged 60 to 64, there was a similarly large rise in part-time working over the 1990s, from 8% to $10^1/_2$% in the Union as a whole, with again most Member States showing an increase except Italy and Luxembourg and, in this case, Denmark, where there had been a large rise during the 1980s (Graph 72). The increase was particularly marked in the UK, where it went up from 11%

to almost 18½%, while in France, where men tend to retire at 60 and very few in this age group are still in the work force, it went up from 9% to 16%.

Older women employed part-time

For women, the relative number working part-time also increases with age, though the tendency is less general than for men. Over the Union as a whole, just under 31% of women aged 25 to 49 in work were employed part-time in 1996, the proportion varying from under 10% in Greece and Portugal to almost 70% in the Netherlands. For women aged 50 to 54, almost 35% of those employed worked part-time. In three countries, however, France, Austria and Sweden, the proportion was less than for the younger age group. In four countries, on the other hand, Ireland, the Netherlands, Portugal and the UK, it was at least 7 percentage points higher.

For women aged 55 to 59, the proportion of those in employment with part-time jobs was just under 40% in the Union in 1996, some 5 percentage points above that for the younger age group, but again in a number of Member States — Belgium, Spain, Italy and Finland — the proportion was lower rather than higher, while in Ireland, it was the same (Graph 73). In Denmark, France and Sweden, by contrast, it was over 8 percentage points higher.

For women, unlike for men, part-time working does seem to contribute to high levels of labour force participation among those in older age groups, as, indeed, it does for those younger. Leaving aside the Netherlands, where relatively low levels of participation are combined with very high rates of part-time working, all of the Member States in which the proportion of women aged 55 to 59 in employment working part-time was above the Union average also had an above average proportion of women in work.

For those aged 60 to 64, only in Belgium and Ireland was the proportion of women working part-time lower than for 55 to 59 year olds, and again the overall figure for the Union as a whole was 5 percentage points higher (at 44%). In 6 Member States, it was at least 8 percentage points higher, in four of these — Austria, Finland, Sweden and the UK — over 11 percentage points higher. Indeed, in the last two countries, over 60% of women in this age group in work were employed part-time, as was the case in the Netherlands, while in Germany, the figure was over 55%. For this age group, however, the relationship between part-time working and labour force participation is less clear-cut, with Greece, Ireland, Portugal and Finland, all combining above average participation with a below average proportion of women working part-time.

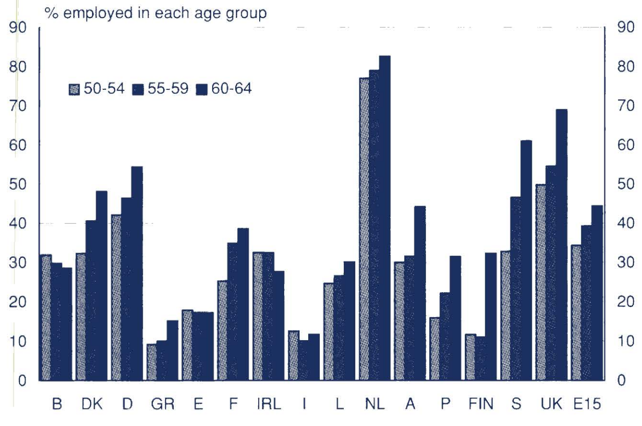
As for men, it is difficult to discern the effect of partial retirement measures on the scale of part-time working among women, though as is generally the case, it is impossible to know what this would be in the absence of such measures.

Changes in part-time working of women

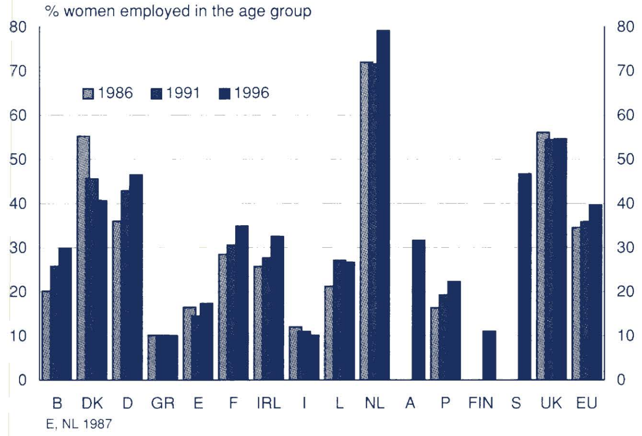
For women aged 55 to 59, the proportion in work employed in part-time jobs in the Union increased from 36% to 40% between 1991 and 1996, more than for younger age groups and more than in the preceding five years. Apart from Italy and Luxembourg, as for men, Denmark, where there was a general fall in the extent of part-time working, and Greece, where there was little change, both for this age group and younger ones, all Member States recorded significant increases, except for the UK, where already in 1991, around 55% of women of this age worked part-time (Graph 74). It would appear that the growth of part-time working may have contributed to more women of this age working. All of the countries where part-time working went up also experienced an increase in participation among women in this age group. Of those where it declined or remained much the same (the UK), only Greece showed a rise in participation over the 1990s.

For women aged 60 to 64, there was a similar increase in the Union during the 1990s in the proportion working part-time as for the 55 to 59 year olds. The rise was general to all Member States, except Italy, the Netherlands and the UK (in the latter two of which the figure was already well above that in other parts of the Union) and, apart from Spain and Ireland, exceeded 5 percentage points (Graph 75). Moreover, as for the younger age group, all of the countries in which part-time working increased significantly, Luxembourg apart, showed some rise in participation of women

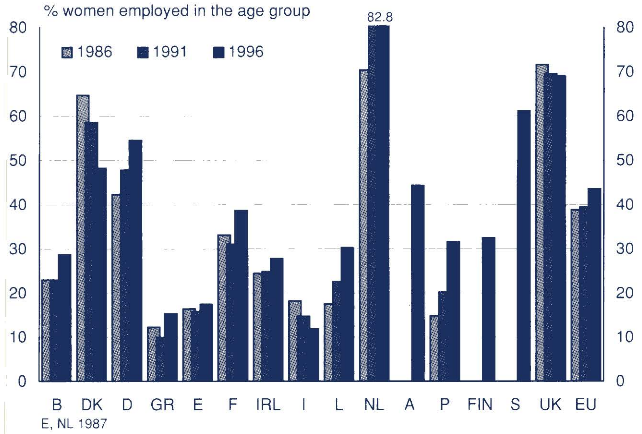
73 Women employed part-time by age group, 1996



74 Part-time working among women aged 55-59, 1986, 1991 and 1996



75 Part-time working among women aged 60-64, 1986, 1991 and 1996



of this age, though in most cases from a very low level.

Concluding remarks

On the above evidence, there does seem to have been a relatively widespread growth in part-time working among older workers over recent years, though it is also the case that this has been true as well of those in younger age groups and it is difficult to attribute much of this to partial retirement policies *per se*. Moreover, much of the growth may have been at the expense of full-time jobs rather than increased numbers leaving the work force completely.

It remains the case, irrespective of the shift in the emphasis of policy, that there is a widespread tendency among companies, forced to reduce employment, to concentrate redundancies on older workers, often with the agreement of trade unions. This is understandable given the larger severance payments which they are frequently entitled to and their often more favourable treatment under the social protection system, in the sense that they are better placed to claim disability benefits or to qualify for various early retirement schemes. At the same time, from the government's perspective, it may be preferable to accept paying larger transfers to these, especially if they are not counted among the unemployed, rather than to pay unemployment benefits to younger workers.

Moreover, there remains an awkward question about the returns from providing training or subsidising employers to do so when the people concerned may be approaching the end of their working careers, especially in the context of constraints on expenditure where to do so may mean cutbacks in other areas. Nevertheless, the case for a more active approach, as for labour market policy in general, remains strong if the welfare of the people concerned and the potential benefits of exploiting the know-how and experience of older workers in the productive process are given adequate weight. It is even stronger in a context where demographic trends are set to increase the number of people reaching retirement age significantly throughout the Union and to reduce the number of young people joining the labour force.

Chapter 6 Health-care: containing costs and improving services

Growth of demand for health care poses a common policy dilemma for governments throughout the European Union, as indeed, for those in other parts of the world. As their real income increases, there is a general tendency for people to want a higher standard of care and to have access to more and better services should they need treatment. At the same time, the ageing of the population in European countries is itself increasing the need for care, while, on the supply side, advances in medical science and in technology are expanding and improving the treatments available. The issue facing governments is how far they should respond to growing demand, and the pressure from health care providers for the delivery of more services, by allowing expenditure on health to rise and, if they seek to limit this, how the limits should be chosen.

Since most expenditure on health care in Europe is part of public sector spending and financed from taxes or social charges, growth tends to conflict with the overall objectives of fiscal policy and with budget constraints, which have generally tightened in recent years. Leaving health care to private sector provision, however, does not resolve the dilemma or absolve government from responsibility for expenditure growth. In the US, where services are mostly provided by the private sector, inflation of health care costs and the associated rise in insurance premiums, which to a large extent are met by employers, as well as in the costs of Medicaid which is publicly funded, is an ongoing source of difficulty for government.

Whereas most other services can be left to market forces to determine the level and pattern of provision and to competition between suppliers to contain costs, the special nature of health care and the priority attached to it by consumers, allied to the difficulty for them of judging quality of service independently of price, are always likely to lead to excessive demand and over-inflated prices. Equally, the free operation of market forces will not necessarily result in those on low incomes receiving the treatment they require, and the pattern of resource allocation may tend to reflect the preferences of those that can afford to pay rather than the true needs of society. In view of this, and in view of the externalities associated with the non-provision of treatment — in the form of exposure to contagious diseases, for example — governments cannot avoid involvement in health care issues and ensuring the provision of at least a basic level of care, though what such basic care should consist of is open to widely different interpretations.

The wide consensus on the need for government involvement in health care provision and on the justification for a measure of control over expenditure growth has not so far, however, led to any general agreement on how the level of provision should be determined. In the European Union, where there is a common commitment to the provision of a high level of essential care available to all irrespective of their income, most governments have, in practice, applied relatively crude criteria to determine how much should be spent — that, for example, expenditure should not increase by more than GDP or that the share of finance going to health services should be kept constant. They have, moreover, generally succeeded in achieving such objectives. According to the latest figures, in most Member States, public spending on health care, and indeed total social spending, has remained largely unchanged in relation to GDP since 1993 and the end of the recession of the early 1990s.

The key issues relate not so much to how costs have been contained — it is not so difficult to keep down expenditure if governments control health service budgets either directly, where the service is part of the public sector, or indirectly, where it is provided *via* insurance funds whose income is state controlled — but to the effects on the standard of service and on the universal availability of care or treatment required. In other words, in a context where health services are rationed, as they are in all countries, the important questions concern the way that the limited resources are allocated, both between different kinds of service and between individuals, how the maximum output from the resources available is obtained and how the system of control — or rationing — applied interacts with these issues.

In practice, governments have tried to deploy market forces to help both to contain costs and to allocate resources more effectively, while, nevertheless, retaining a large measure of control. Most commonly, direct charges have been imposed, or increased, on pharmaceuticals and certain kinds of treatment to reduce the cost falling on the state and to curb demand. In addition, in many countries, efforts have been made to distinguish more clearly between demand and supply, between purchasers of services (private individuals, insurance funds and GPs) and providers (hospitals, specialists and analysts) in order to create the conditions for market forces to operate. These include efforts to break the link between treatment and remuneration and to reduce the possibility of practitioners being able to over-prescribe treatment in order to increase their income (which remains a problem where fees are paid on a case-by-case basis). Such efforts have been accompanied by attempts to introduce the possibility of competition between both purchasers and providers so as to realise the potentially beneficial effects of market forces on efficiency.

In all cases, however, such attempts have run up against the limitations to competition inherent in a managed market for health care, where the maintenance of local centres of treatment is important and where there can be significant economies of scale (in hospitals providing a full range of specialist services or in insurance funds with subscribers who have a wide range of characteristics, for example). In practice, governments have generally been unwilling to allow competitive forces to have full reign and their effect on efficiency has, therefore, been extremely muted.

Nevertheless, there have been apparent gains to the introduction of market, or pseudo-market, mechanisms, as indicated below, though these largely seem to have come from the reorganisation itself, the measures taken as a corollary of this and the disturbance of cosy bureaucratic relations between the main protagonists, which tended to distort priorities and objectives. In particular, the division between purchasers and providers, allied to the specification of precise budgets, opens the way for the establishment of more commercially-oriented relationships between the two sides and for the formulation of contracts defining the services to be supplied over specific periods of time and the terms and conditions to be applied. It also provides greater scope for the exercise of managerial responsibility and increases the importance both of good management and of systematic information about the costs associated with different kinds of treatment or service. Moreover, it tends to shift the balance of power from providers to purchasers, so giving a greater voice to consumers and according more weight to their interests.

By increasing cost effectiveness, the introduction of these kinds of measure in some countries seem to some extent to have offset the effect on service provision of the increasing restraint of expenditure on health care. There are signs in a number of Member States, however, of a relatively high level of dissatisfaction with public health services and a widespread desire for improvements and extended types of treatment and preventative measures. It is open to question whether these can be realised by efficiency gains alone within the constraints which have been imposed on expenditure, or funding, growth.

Outline of analysis

The concern in this chapter is not to review the changes in systems of health care which have occurred in all the Member States in the recent past but to focus on selected countries where substantive reforms have been attempted or contemplated. These are intended to be illustrative of the direction of change across the Union and the implications of this. The countries chosen for study are:

- the UK, where the changes implemented by the previous government have attracted much attention in other parts of the Union because of the attempt to introduce pseudo-market mechanisms into a publicly-operated service;

- the Netherlands, where extensive market-based reforms were proposed some years ago but have been implemented only very gradually and where a more conscious effort than elsewhere in the Union has been made to define the services which should be publicly provided and those which can be left to the private sector to supply;

- Germany, where significant direct charges have been imposed on patients in an attempt to curb the rise in social contributions;

- France, where expenditure on health care is among the highest in the Union in relation to GDP and where efficiency in service provision has been tackled through regulation rather than competition;

- Italy and Spain, which have similar regional structures of health service organisation and where similar kinds of change have been introduced to overcome problems of inefficiency.

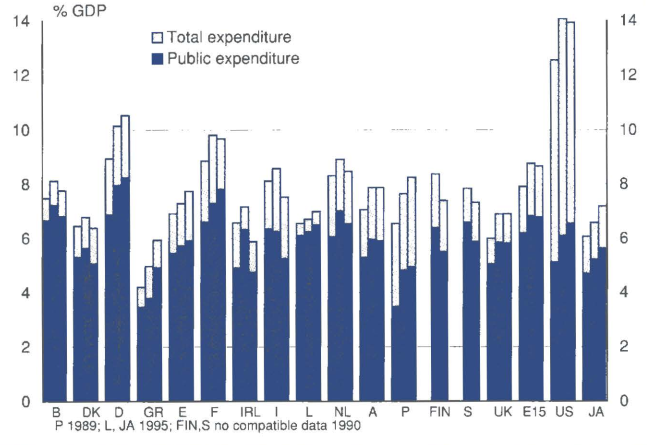
These countries are examined in turn below. First, however, trends in expenditure on health care in recent years are reviewed in order to provide a quantititative background to the analysis. This is based on OECD data rather than on ESSPROS figures as deployed elsewhere in this Report, since these cover developments in the private as well as the public sector. In practice, however, for most countries, although there are some differences because of differing definitions used in the scale of expenditure, the changes shown by the ESSPROS data are similar to those shown by the OECD figures for public spending on health.

Trends in health expenditure

Total expenditure on health care in the Union amounted to just under 9% of GDP in 1996, the figure varying from 6% in Greece and Ireland to just under 10% in France and $10^1/_2$% in Germany (Graph 76). These figures are substantially below that in the US, where spending was equivalent to 14% of GDP, though mostly above that in Japan, where it was just over 7%. Over the 1990s, expenditure in the Union has risen by almost 1% of GDP — less than in the US or Japan — and, as for total spending on social protection, all of the rise occurred in the three years of recession at the beginning of the period, reflecting in large measure the lack of growth in GDP.

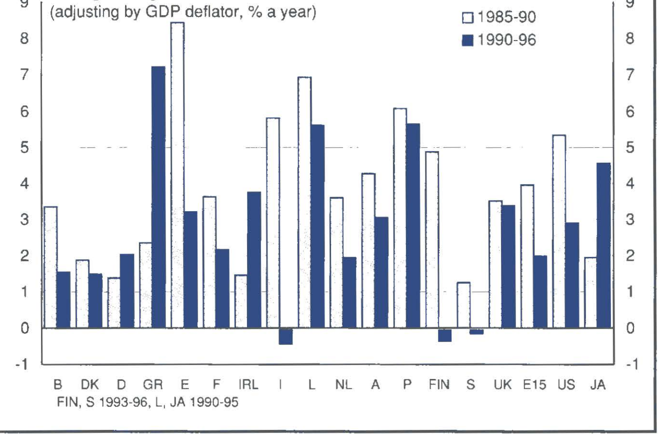
Indeed, spending in real terms (adjusted for general inflation) in the Union grew by only around 2% a year per head of population between 1990 and 1996 (and by less in volume terms — ie adjusting for the rise in health costs), half the rate over the preceding five years (and about the rate required simply to keep pace with the ageing of the population — see Chapter 1). Growth in Greece and Portugal, however, where the service is less developed than elsewhere, was significantly higher than average

76 Total and public expenditure on health in relation to GDP in Member States, the US and Japan, 1990, 1993 and 1996



P 1989; L, JA 1995; FIN,S no compatible data 1990

77 Change in health expenditure per head in Member States, the US and Japan, 1985-90 and 1990-96



FIN, S 1993-96, L, JA 1990-95

(over 6% a year in real terms), as it was in Ireland and Luxembourg, while at the opposite extreme, real spending declined slightly in Italy, Finland and Sweden (Graph 77).

Public expenditure on health in the Union accounts for just under 80% of total spending, much the same as in Japan, but considerably higher than in the US (around 45%). Perhaps surprisingly, however, public expenditure on health in the Union in relation to GDP is not significantly different from that in the US (around 6$^{1}/_{2}$%). In most Member States, the relative scale of public spending is close to the Union average, the only exceptions being Belgium and Luxembourg, where it is around 90% of the total and Italy and Portugal, where it is around 70% and 60%, respectively. There has, moreover, been very little change in the relative weight of the public sector during the 1990s, except in France, Ireland and Portugal, where it has risen, and Italy, Finland and Sweden, where has fallen (though since for some countries the OECD data fluctuate alarmingly from year to year, trends can be difficult to discern). Except in the latter three countries, there is little sign, therefore, that the constraints imposed on the growth of public spending on health care across the Union have led to any significant increase in private expenditure.

Health care reform

UK

Up until 1991 when significant reforms were introduced, the national health service in the UK can be characterised as a 'command and control' bureaucracy, where hospitals were owned and operated by the State, which also employed the staff, and though general practitioners (GPs) were self-employed, they contracted most of their services to the NHS. In macro-terms, the system had cost-effective features — in particular, governments could exercise firm control over expenditure and, unlike in most other countries, doctors and specialists were not paid on a fee-for-service basis and so had no incentive to under-treat and artificially boost demand — and spending was comparatively small in relation to GDP (in 1990, public expenditure was around 5% of GDP, lower than in all other Member States, apart from Greece, Ireland and Portugal).

At the same time, however, an absence of costing mechanisms together with clinical freedom meant that, in micro-terms, resources were not necessarily used in the most cost-effective way and their allocation between different types of care or treatment was largely historically determined and unresponsive to the interests of patients. Moreover, waiting lists were the primary means of rationing available resources between patients and these lengthened as restraints on expenditure were tightened, so reinforcing the pressure for change.

The reforms introduced in 1991 were designed to tackle the latter kinds of defect, while maintaining the essential principle of the NHS, that it be available for all regardless of income, and retaining the same means of centralised control over expenditure and the same method of funding from general taxation. Their main feature was the introduction of a quasi internal market, with separation between purchasers (District Health Authorities and GP fund-holders) and providers (hospitals and other service centres) and with the latter competing for shares of the budgets controlled by the former.

District Health Authorities (DHAs) were allocated budgets to purchase services based on the size and characteristics of population in their areas; while GPs with practices above a certain size were given the option of becoming fund-holders with budgets to purchase a more limited range of secondary care for their patients. Hospitals and other providers could opt for a more independent status and were given more discretion over pay, skill-mix and the delivery of services, the intention being that they should contract with purchasers over supply (with a number of different types of contract being possible, ranging from agreements to pay a fixed sum for a specific period irrespective of volume to those specifying a fee per patient). By April 1996, almost all health care providers had become independent trusts and 50% of GPs, covering 52% of the population, had become fund-holders.

Before the present Government took office in 1997, the principal development since 1991 had been the extension of GP fund-holdings to smaller practices and an increase in the range of services they were allowed to purchase, with the largest practices (around 80 altogether) being given budgets to cover all hospital and community services.

The effects of the reforms are difficult to evaluate because of other changes introduced during the period and the expansion of the health care budget (from 5% to around 6% of GDP). Nevertheless, the evidence available suggests that there have been some gains in efficiency, though less than the advocates of the reforms had hoped for, without any discernible deterioration in the quality of service.

A marked feature of the changes introduced has been the large growth in managers and administrators (though the precise figure is difficult to estimate because of the reclassification of staff), which has resulted in the cost of administration rising from an estimated 8% of total expenditure before the reforms to 11% or so at present. The Department of Health index of health service activity (or output), however, has risen by more since 1991/92 than before (by some 4½% between the 1991/92 and 1995/96 financial years as against just over 2% between 1979/80 and 1990/91), while costs have increased by less than in proportion (by just over 2% in the second period as against just over ½% in the first). Estimated productivity growth on this measure (which, it should be emphasised, takes no account of service quality) has, therefore, been higher since the reforms than before (by almost 1 percentage point a year).

At the same time, information flows, especially on costs of different kinds of treatment or care, have improved dramatically and, as a result, there is undoubtedly more awareness of the expenditure implications, and opportunity costs, of medical decisions, which has almost certainly led to improvements in resource allocation.

The effect on access to treatment is more uncertain. Although the number of people waiting for admission to hospital or out-patient treatment was higher in March 1997 than in March 1991 (some 1,164 thousand as against 948 thousand), the average waiting time was significantly less (1½% had been waiting for over one year in September 1996 as opposed to 16½% five years earlier, though average waiting time has increased since then). The latter, however, is the result of policy initiatives specifically aimed at reducing waiting time as well as, possibly, of the reforms. Equally, there is mixed evidence on inequalities in access to treatment between those living in different parts of the country or registered with fund-holder GPs as opposed to others.

In terms of quality of service, public surveys indicate an increase in satisfaction with the NHS as a whole during the early 1990s, following a significant decline during the 1980s, but a renewed decline since 1993, virtually back to the 1990 level by 1995. This seems to centre very much on inpatient care in hospitals, whereas there has been a rise in satisfaction with outpatient treatment and a consistently high level of satisfaction with GPs. Moreover, there appears to be a wide consensus among analysts that the shift in the balance of influence over service provision to GPs has had a beneficial effect on quality and that these have proved to be more effective in purchasing secondary treatment than DHAs, partly because of their smaller size and the more personal service they can provide. Indeed, DHAs have not been able to use their larger size effectively to elicit improved services from providers — which was an important objective of the reforms — either because many of these are in practice local monopolies or because of the political difficulties of shifting from one supplier to another, especially where this would create financial problems for the provider losing business.

The present Government in the UK, which was critical of the internal market when in opposition, announced its intention, at the end of 1997, to reform the system further by effectively abolishing the — limited — competition which exists and introducing cooperation in its place, though while retaining the division between purchasers and providers. It is planned to give responsibility for purchasing secondary care in local areas to new primary care groups in place of fund-holding GPs and DHAs, which will have the task of setting three-year strategic plans and of monitoring standards. These groups will be composed of GPs, nurses and other local professionals and each will cover around 100 thousand patients, a major aim being to encourage GPs to treat more patients themselves, so taking pressure off over-crowded hospitals and reducing costs. Instead of competing for patients, hospital trusts will be required to meet unit-cost ‘benchmarks’ and those that fail to do so may lose control over their affairs either to their NHS region or to a new Commission for Health Improvement set up to carry out cost and clinical audits.

The potential dangers of such changes are, first, that the balance of power may shift back more to providers because of the inability of purchasers to shift between alternative suppliers and, second, that the primary care groups will be too big to provide the same kind of personal service as fund-holding GPs but too small to influence providers.

Netherlands

Reform of the Dutch health care has occurred in a more gradual and piecemeal way, with similar objectives to those in the UK but from a different starting position (ie one where there was no national health service as such but where the purchase of care, though predominantly state-financed, was organised through insurance funds). The initial proposals for change were made by the Dekker Commission in 1987. These were revised slightly by a new Government in 1989 in what became known as the Simons Plan and then modified more substantially by the present Government from 1994 on. The Dekker-Simons proposals had two main components: first, a compulsory comprehensive national health insurance scheme in place of the existing segmented financing system to guarantee universal access to basic services and, secondly, managed or regulated competition between both health insurers (ie purchasers) and providers to stimulate improvements in efficiency.

Under the proposals, national health insurance was to be financed by income-related contributions, administered by a statutory body and distributed to health insurance funds according to both the numbers registered with them and their average risk of requiring treatment so as to prevent 'cream-skimming' (ie funds concentrating on the healthiest sections of the population). Accordingly, retrospective reimbursement of the expenditure incurred by individual funds was to be replaced by prospective budgeting, with a fixed fee per 'standard' person insured providing an incentive to contain costs and improve efficiency as the means of increasing profit. In addition, the fee was to be set below the average expected costs and supplemented by a flat-rate premium paid directly by the person insured, so as to provide a further stimulus to efficiency, since the more successful a fund was in containing costs, the lower it could set this premium and the more clients it would attract.

Insurance funds were to be given freedom to contract with approved providers and to negotiate terms with them, while regulation of prices and of hospital capacity was to be lessened to give funds more scope for influencing costs. Providers were to be free to compete for contracts, just as insurance funds were free to compete for subscribers, with consumers being able periodically to switch between funds, which, in turn, were obliged to accept any applicant. At the same time, the strict division between purchasers and providers was to be relaxed to allow the development of alternative delivery systems.

In practice, the two main components were far from being implemented in full, though there was a significant shift towards managed competition. Insurance funds were able to contract selectively with health-care professionals and compete for subscribers, as well as to charge a premium according to the community they were serving, enrol subscribers from outside their region and negotiate fees with providers below those officially approved. From 1993 on, funds received a prospective budget based on the number of subscribers, but only very partially adjusted for the risk of them requiring treatment — specifically only for age and sex. This was considered too crude to make funds fully liable for the expenses incurred and they were, therefore, compensated for 97% of any losses they made, while being required to refund 97% of any surpluses, so effectively removing both any risk and any incentive to contain costs.

In 1995, the effects of the system were assessed by the Sickness Fund Council, which found that funds were not exercising their option to contract selectively with providers or to negotiate lower fees. It concluded that the main effect of reform was to encourage mergers between insurance funds and hospitals and to reinforce collaboration between providers. It attributed the lack of competition to an absence of adequate financial incentives for insurance funds and to collusion between providers and purchasers, induced partly by successive reductions in Government-approved fees.

The present Government's response was the publication of plans in 1995, abandoning the goal of comprehensive basic health insurance and retaining a segmented system but aiming to reform the incentive structure. The financing system was divided into three components covering different types of service and each with their own regulatory regime:

- long-term and mental health care, financed by national health insurance (AWBZ), with a single purchaser in each region and with regulation of prices and supply by Government;

- basic curative care, financed by mandatory health insurance, with sickness funds and private health insurers being responsible for purchasing treatment and with managed competition between both these and providers;

- amenities and inexpensive care, financed by voluntary health insurance, with sickness funds and private health insurers again being the main purchasers and with a free market on both the demand and supply side.

In practice, as regards the first component, administration of care is planned to pass from the insurance funds to a single purchasing authority in each of the 27 health regions, which is likely to be the largest sickness fund in each case. There will, therefore, be no possibility of competition between insurers, while the control of expenditure exercised by regulation of prices and supply of services will leave little scope for competition between providers, with two exceptions. First, as noted in Chapter 7, very limited funds (3% of the total budget for home care) have been allocated since 1995 to people requiring care at home to purchase care from relatives or friends rather than professionals if they wish. Secondly, 5% of the home-care budget has been set aside for traditional regional organisations and other officially-recognised agencies to compete for. The initial plan was that this should increase to 35%, but a lack of adequate rules to manage competition and the prospective large-scale entry of commercial organisations have caused a postponement of any increase until 2001 (there is, nevertheless, some evidence that the limited competition has already stimulated higher productivity among traditional carers).

For the second component, basic curative care, the changes are in line with the initial Dekker-Simons proposals. Within a few years, insurance funds are to be paid prospectively, rather than retrospectively, for all the medical care they purchase — by 1997, the prospective proportion had been raised from 3% to 27% — in order to increase their financial risk and encourage them to purchase more cost-effective care. This has been accompanied by the introduction of new criteria for adjusting their *per capita* fee, taking account of the region of residence and disability status of subscribers. There are already signs that the changes are stimulating increased competition (in 1997, there was a difference of 40% between the highest and lowest flat-rate premiums charged by funds to subscribers as against 10% in 1996) and greater efforts to contain costs (such as through greater coordination of referrals by GPs to specialists, the development of lists of preferred providers and the provision of more information on costs and resource use to doctors).

In addition, plans have been announced to deregulate the prices for treatment and to remove controls over capacity (except in the case of large hospital investment), giving the insurance funds responsibility for negotiating prices with providers and enabling the latter to plan the development of facilities. (At present, providers are paid on a fee-for-service basis, the fees being set by Government and adjusted downwards the following year if expenditure exceeds the initial target.)

At the same time, the Government has introduced a scheme fixing maximum prices for groups of registered drugs, equal to their average price in Belgium, France, Germany and the UK, which has already yielded significant cost savings. Moreover, limited user charges have been introduced to encourage people to use services more prudently (a charge per hospital day and a 20% fee for all other treatment except visits to GPs, with the charge any individual pays over a year being limited to 200 guilders — around 90 ECU — and with concessions for the chronically ill). The complexity of the scheme, however, seems to be resulting in heavy administrative costs, which could outweigh the revenue collected.

For the third component, amenity care, the intention is to remove any regulations governing provision or financing of the services, since collective responsibility — and their availability as part of the social protection system — is no longer deemed necessary. The scope of this component has been defined in terms of the treatment or services included not being medically necessary, or necessarily effective, and being affordable. These are difficult criteria to apply in an objective and non-controversial way, as has proved to be the case in practice. So far very few items have been included. In 1995, dental care for adults and in 1996 some physiotherapy treatments were transferred from basic curative care to amenity care. Since people with bad teeth, however, experienced serious problems in obtaining affordable insurance cover for false teeth, this item was transferred back again in 1997 following considerable political pressure.

Germany

The German health care system is similar to the Dutch one, in that insurance funds are responsible for purchasing treatment and services from providers, though unlike in the Dutch case, finance comes predominantly from social contributions levied on employers and employees. The overriding concern in recent years has been to limit the rise in contribution rates, which are a significant element in non-wage labour costs, without damaging the high standard of care which prevails (overall expenditure on health care is the highest in the Union in relation to GDP). The two main pieces of legislation to reform the system, which were introduced in 1988 and 1992, were aimed at achieving this, essentially by endeavouring to limit expenditure to the income received from contributions.

In both 1995 and 1996, however, the deficit on health care amounted to around 6–7 billion deutschmarks (3–3½ billion ECU) prompting a further step in the reform process. Competition between insurance funds for members has been introduced, but perhaps the main aspect is a shift from contributions to direct charges levied on patients who already pay significant fees (covering 20% of spending on drugs), the intention being to increase the total amount collected in direct charges — to around 6% of total expenditure to enable average contribution rates to be reduced once the deficit has been eliminated. Such copayments, in addition to being indexed to keep pace with wages, are planned to be linked to insurance premiums — each 0.1 percentage point rise in premiums leading automatically to an increase of 1 deutschmark in copayments. As a result, the share of health costs met directly by patients is set to rise significantly in future, though provision for the relief from charges for the chronically ill and the poor has been extended.

The intention is that linking charges to premiums in this way will put pressure on insurance funds to hold down costs to avoid having to raise contribution rates, which could lose them members since these are allowed to shift from one fund to another whenever rates are increased. At same time, however, a number of cost control measures have been abolished, such as provisions for controlling drug prices, or modified, such as regulations governing the prescription behaviour of doctors and their remuneration, which seem likely to make it more difficult to monitor and control budgets and harder for insurance funds to contain costs and premiums.

Although the intensification of competitive pressure on insurance funds might lead them to introduce stricter measures to control costs and adopt tougher bargaining positions in their negotiations with health care providers, in practice, it proved impossible to implement the link between premiums and direct charges in 1997 and, as it is an election year, political considerations suggest that it will not be fully implemented in 1998 either. Nevertheless, the figures for expenditure in 1996 seem to indicate that insurance funds have begun to make greater efforts to reduce costs.

At the same time, looking beyond the preoccupation with contribution rates, there are signs of a shift in the orientation of policy, towards giving more weight to the growth potential of the health sector and to the evident desire of many people for higher quality and more innovative services, which they seem willing to pay for. A new provision of legislation, therefore, gives insurance funds an ability to expand the range of benefits they provide, though any such expansion has to be financed entirely by those insured and not by employers, who at present account for just under half of contributions.

France

The health system in France is similar to that in Germany, with insurance funds financed mainly from contributions responsible for purchasing services from a mix of public and private sector providers. As in Germany, expenditure is high relative to GDP and the public component of this, in particular, has continued to grow significantly during the 1990s, giving rise to significant deficits which policy has been aimed at reducing, though so far without much success.

In the case of ambulatory care (ie non-hospital in-patient care), charges are on a fee-for-service basis, with rates negotiated between doctors' organisations and insurance funds (*Caisses nationales*). Patients pay the total price and then receive refunds from the national insurance funds of between 40% for 'comfort' drugs and 75% for consultation. If they are insured under a private scheme (which 87% of the population are), they can also receive a refund, either full or partial, to cover the remaining amount (the *ticket modérateur*). Around 10% of patients are exempt from charges because of long-term illness, while extra charges are payable if so-called *Secteur II* specialists are consulted.

Patients have direct access to care through four different points of entry — GPs, specialists, hospital out-patient departments and the emergency services — and the only restraint on their demand is the *ticket modérateur*, the effect of which is reduced if the person has private insurance. On the supply side, the only response to spending increases has been to freeze fees, but the effect of these can be circumvented by doctors over-prescribing or stipulating return visits and unnecessary examinations. Moreover, GPs who face direct — and, in some degree, unfair — competition from specialists may readily agree to over-prescribe drugs or give certificates for time off work.

In 1992, a *Caisse Nationale* report identified inefficiencies in the system, estimated at up to 10% of the total budget, and argued that, because of the problems indicated above, these could be reduced without fundamentally changing the system, by more systematic use of evaluation methods and clear definitions of standard practices rather than by limiting fees or increasing direct charges.

In the case of hospitals, patients are free to choose between the two-thirds which are public and the one-third which are private, both of which are covered by national insurance. Investment has been planned centrally since 1970, and public hospitals have been subject to global budgeting since 1984, which has curbed growth, but which has had a limited effect in encouraging greater efficiency since any surpluses they make are claimed back. Private hospitals continued to be reimbursed on a fee-for-service basis up until the 1990s, resulting in a shift of activity to these.

The system generates inequalities between patients insofar as entitlement to benefit is related to professional activity rather than medical need. Those not covered by private insurance tend to be the poor and elderly and while social assistance gives them free entitlement to health services, because they have to pay the full cost of consulting with a GP or specialist before receiving a refund, this leads them to use public hospitals more frequently and postpone treatment. In addition, direct charges have increased to cover almost 31% of total ambulatory expenditure in 1996.

During the 1990s, emphasis has focused on performance-related regulation of supply rather than competition between providers, as in the UK or the Netherlands. Global budgeting has been extended to private clinics and treatment centres, with these having to pay back insurance funds if they overspend or into a special fund if they underspend. In addition, since 1994, indicative aggregate levels of spending on drugs have been negotiated with pharmaceutical companies in place of the previous system of fixed prices, which because they were low encouraged over-prescription, while prescribing guidelines have been set for individual doctors to follow, with the possibility of financial sanctions if they exceed them. Though caps on expenditure have succeeded in restraining growth, experience demonstrates the importance of good information systems to help determine targets and for monitoring performance.

The Juppé Plan of the previous Government, announced in 1995, endorsed the view that control should shift from trying to limit demand to regulating the performance of providers, though no changes were proposed to the fee system for doctors or for restraining patient demand. The main aims were:

- to widen the contributions' base by raising social charges on the unemployed and pensioners (from 1.4% to 2.6%) and to increase the share of funding from taxation by extending the CSG (*Contribution Sociale Généralisée*) to health care;
- to improve coordination between the State, insurance funds, local health authorities and representatives of health care professionals;
- to regionalise expenditure targets;
- to improve systems of information;
- to improve continuity of care through better patient records and

the quality of service by making further education for doctors compulsory;

- to improve evaluation and accreditation of hospitals and the regional allocation of funds;

- to stimulate increased productivity in hospitals by varying their target rates of expenditure growth and reducing disparities between public and private hospital care.

Though the plan has proved deeply controversial, the process of increased regulation of professional activities is likely to continue and, after many years of short-term cost containment, reforms of a more structural nature seem to be in prospect.

Italy

A national health service (SSN), on essentially UK lines, was established in Italy in 1978. Unlike in the UK, funding came mainly from social contributions and though there have been plans to shift entirely to a tax-based financing system, they still account for almost half of total revenue. Like in the UK, however, by the early 1990s, though health expenditure was not excessive in relation to GDP (at around the Union average), there was growing dissatisfaction with its overly bureaucratic and complex administrative features, which resulted in cumbersome decision-making unresponsive to patient needs, inefficient resource allocation and deficient audit mechanisms.

Though some 25% of the SSN's budget went to purchase services from outside providers, there was little attempt to use its potential bargaining power to stimulate greater efficiency or quality improvement. Payments were generally on a fee-for-service basis or based retrospectively on costs in the case of public sector providers. Inefficiencies were exacerbated by the fact that both the Ministry of Health and the regions were formally responsible for planning and regulation, making it difficult for the centre to control not only the allocation of resources within regions but also their overall expenditure. (The Constitutional Court declared it illegitimate for central government to make regions responsible for exceeding the spending limits set, so giving them no incentive to respect these limits or contain costs.) As a result, the deficit on health care averaged 12% of expenditure between 1987 and 1992. The response of Government was to freeze employment, impose tight limits on capital spending and deliberately underfund the service, which served to aggravate the efficiency problem further.

The reforms introduced in 1992–93 were aimed at improving expenditure control and efficiency. Organisational and administrative responsibility for health care was transferred to the regions and a ceiling was set on the Government's contribution to regional funding (the amount in each case considered necessary to ensure uniform levels of care less revenue from compulsory contributions attributable to the region), any spending in excess of this needing to be financed from a region's own resources — either from direct charges or from increased contribution rates (within centrally-set limits). As a result, the richer regions receive little or nothing from Government, the poorer ones up to half of their total budget. In general, the effect has been to persuade regions to stay below their spending limits. In the longer-term, however, it could give rise to wider differences in services and, because of the small amounts transferred to richer regions, weaker State influence over the care provided

To stimulate greater efficiency and more attention to quality of service, following the example of the quasi-market mechanisms introduced in some other Member States (especially the UK), measures were taken to separate purchasers and providers and to encourage an element of competition. To reduce bureaucracy and improve management, the existing 659 Local Health Units were transformed into 228 Local Health Enterprises (LHEs), with more operating autonomy, commercial accounting procedures and performance auditing and administered by senior managers appointed by the region for fixed terms with performance-related salaries. In addition, 90 large hospitals were transformed into Hospital Enterprises, independent from LHEs and administered by contracted senior managers, and, while other health facilities continue to be managed directly by LHEs, the intention is that they should have operating autonomy.

In practice, the implementation of the measures has been slow in some regions and, though managers are well paid, few have come from the private sector. Nevertheless, improvements in efficiency are already evident in many LHEs and Hospital Enterprises and relations with patients seem to have improved (national surveys suggest that satisfaction levels have risen), partly as a result of the compulsory publication of Service Charters, setting out patient rights as regards, for example, waiting times, access to information and complaint procedures.

In principle, patients have the right to choose between providers, public or private, accredited by the regional authorities, which are responsible for setting fees in line with national guidelines and which have wide discretion over the form which competition between providers takes. This has varied considerably between regions, though in many cases priority has been given to expenditure control and planning, leaving little scope for competition between providers and limited freedom for patients to choose between them. In such cases, the danger is that the *status quo* will be maintained and the separation of purchasers and providers will be largely illusory. In a few regions, however (such as Lombardy), competition between providers is being actively encouraged.

At the same time, the latter development might weaken expenditure control if providers are no longer regulated. While in all regions, mechanisms have been introduced to combat the tendency for fee-based payment systems to encourage overtreatment by penalising levels exceeding those negotiated, little consideration has so far been given to the potential use of detailed contracts to regulate providers. Moreover, although regions have the power to increase and extend direct charges for services — and although charges were raised significantly by the centre in the 1990s to curb expenditure — no region has so far used this power.

A more recent form of control is the drawing up of approved lists of drugs and treatments which can be prescribed. Though these at present are fairly comprehensive, they may be less so in the future (the 1997 Finance Act contained a series of measures to encourage responsible prescription behaviour by doctors, with guidelines for treating specific ailments, while, in Emilia-Romagna, a basic package of services has been defined). As the imperative for curbing expenditure diminishes, attention is likely to focus more on the way that resources are allocated and increased efficiency is stimulated, as well as on equality of access to services both between individuals and regions.

Spain

A national health service — the *Sistema Nacional de Salud* (SNS) — was introduced in Spain in 1986. Public sector capacity was expanded to improve access to hospital care in rural areas and the organisation of primary care, while the shift to tax-based financing was accelerated (though around 15% of income still comes from social contributions) as was the transfer of power to the regions. For the rest of the 1980s, expenditure increased substantially, regional budgets being determined largely by past spending with little incentive for restraint. Despite this growth, waiting lists lengthened, patient satisfaction was at a low level and there was mounting concern about inefficient management. The main concern, however, was to control expenditure and to reduce the growing budget deficit. In the *Programa de Convergencia*, measures for structural and management change were set out with the aim of reducing spending on health care by 1% of GDP, initially covering the period 1992 to 1996 and subsequently extended for a further four years.

Under the programme, the overall health care budget is linked explicitly to GDP growth, while the allocation between regions is based largely on population (though it is generally agreed that age composition, patient mobility and medical teaching costs should also be taken into account). Regions have undertaken to avoid incurring deficits but have been given greater powers to levy taxes so as to supplement revenue from Government, encouraging at the same time a more responsible attitude to spending growth.

In addition, measures have been introduced in a number of regions, as well by the central health authority (INSALUD which is responsible for managing health care in smaller regions), to increase efficiency and the quality of care. In Catalonia, and some other regions, contracts with GP cooperatives specifying terms for the supply of services have been developed together with the integration of primary care teams with hospitals. In Valencia, long-term monopoly concessions have been granted to private operators for the provision of hospital care. In Catalonia, Galicia and Andalusia, some hospitals have been converted into public foundations or public enterprises to give them greater managerial flexibility and autonomy. INSALUD has introduced a system of *Contrato Programa* (programme agreements) to regulate relations with hospitals, with an activity index being used to prevent the provision of care from being distorted by *per diem* fees. As yet, however, there has been little or no explicit attempt to establish competition between providers.

At the same time, innovation has met resistance. In Andalusia, an attempt to introduce private management of public facilities was blocked, as was INSALUD's plan to introduce quasi-markets in all the regions which it is responsible for. Overall, there has been patchy implementation of new management techniques, which have so far failed to bring about significant organisational change. Nevertheless, programme agreements seem to have raised efficiency in the hospitals concerned, while satisfaction with the SNS among patients is reported to be increasing. This, however, may be due to a shortening of waiting lists caused by a specific government programme to treat by the end of 1996 all patients who had been waiting for over a year (only 5% were not treated), as much as to their greater freedom to choose GPs and specialists and other changes associated with the reforms.

Limited use has so far been made of direct charges, except in respect of prescribed drugs for which a fee of 40% of the price has been charged since 1978, people retired being exempt. Proposals to withdraw this concession and extend copayment to other services have been strongly opposed. Positive and negative lists of drugs and services (ie those which can and cannot be prescribed), however, have been developed and measures introduced to encourage responsible prescription behaviour and treatment on the part of doctors.

While the measures introduced in the early 1990s seem to have curbed expenditure growth (growth in real spending over the period 1990–95 averaged 3% a year as opposed to over 8% a year over the preceding five years) and led to some incentive to increase efficiency, problems remain over the formula for allocating funds between regions, which needs to take proper account of underlying differences in patient characteristics. Moreover, with the greater autonomy given to regions, differences seem to be arising between them in the relative weight attached to equity as opposed to efficiency considerations. Just as in Italy, therefore, concern in the future could well shift away from expenditure control *per se*, to questions of the nature of care provided and equality of access to this.

Chapter 7 Social protection and long-term care

As indicated in Chapter 1, the relative number of elderly people of 65 and over in the European Union is larger than ever before and is set to continue increasing over future decades. As has been widely discussed, this has implications for the growth of social transfers in the form of old-age pensions, which, as noted in Chapter 2, has become a focus of policy concern in all Member States. However, as also noted, the implications for social protection are not confined to old-age pensions. Since an increasing proportion of those drawing pension are living longer into old age and as they get older many of them will become frail or invalids dependent on others, the potential effect on the need for long-term care is equally important.

Although no precise figures are available, it is estimated that around 5% or so of people of 65 and over in the Union are dependent on almost continuous care and a further 15% partly dependent, while for those of 75 or over, the corresponding figures are 10% and 25%, respectively. Moreover, whereas more people are living longer and their general health has, on average, improved significantly over the years, there is little sign that the proportion of elderly in need of care is diminishing, partly because advances in medical science mean that more life-threatening ailments can be kept at bay. The projected high rate of growth of the number of people of 75 and over in the Union — of over 2% a year over the next 25 years — and perhaps even more relevantly of the number aged 85 and over — almost 2½% a year — therefore, implies a marked increase in old-age dependency. If the present mean population projections prove correct, then by 2010 there will be over 40% more people of 85 and over in the Union than in 1995 and by 2020, almost 80% more.

At the same time, social and economic developments (highlighted in Chapter 1) have led to the break-up of the extended family, more people living alone and more women pursuing working careers. In consequence, it is increasingly difficult, particularly in Northern Member States where these trends are most pronounced, for care to be provided from within the family as it traditionally has been. These trends, however, have coincided with a growing recognition of the benefits of providing care at home, if at all possible, rather than in nursing homes or similar institutions. Accordingly, the increasing need for care is, in practice, giving rise to an expanding demand for support services and facilities to enable people to be cared for in their own homes and to help family members, often in paid employment, to provide this.

The main debate across the Union at present centres on how far the state should be involved in the provision of support, in the form not only of social services but also of social transfers to help cover the costs involved in caring, and how far, on the contrary, it should be left to individuals — and families — to make their own arrangements. In other words, the question is whether long-term care should be provided on a market or non-market basis. If the latter, the additional issue concerns the role of the state and whether it should operate as a service provider, purchaser of services or simply as a regulator of private suppliers. The terms of this debate and its focus vary considerably between Member States reflecting the very different ways in which caring needs are currently met and the extent to which they are included within the scope of the social protection system. Indeed, as indicated below, there is a vast difference between the extensive state support available, for example, in the Nordic countries to assist with most caring needs and the situation in much of the South of the Union, where caring is still predominantly carried out within the family.

Nevertheless, the same kinds of issue are relevant in all Member States and are becoming increasingly pressing as caring needs expand. Irrespective of the current situation, governments cannot avoid having a policy on how these needs will be met, if only because ultimately, given the nature of European society and the commitment to a comprehensive system of social protection, the state is the provider of last resort. While they might choose to leave the responsibility for arranging care to individuals, they may still be obliged to provide income and other forms of support if individuals are unable or unwilling to exercise this responsibility.

Although people may be able to take out private insurance to cover the costs of providing care which they might face, they may not choose to do so or may fail to take out a sufficient amount. Unless insurance is made compulsory, which is tantamount to imposing taxes or social charges to finance the provision of care, the state cannot easily limit its responsibility, which is likely to manifest itself in increased expenditure on income support and social services. Moreover, since the distinction between caring needs and health care is not clear-cut, especially for frail elderly people whose continued health depends on them receiving sufficient care, an inadequate response to the former could well result in an increased demand for the latter. Indeed, in all Member States, providing care to the elderly accounts for a large share of health service budgets (between around a third and a half according to estimates).

In addition, concern with social cohesion, as well as with poverty *per se*, implies that governments across the Union cannot ignore the distributional consequences of leaving long-term care needs to personal responsibility. This is all the more so since the need tends to be greater among the poorer sections of the community, who are not only more likely to face the often substantial costs involved in providing care over a long period but are also likely to have to pay higher premiums for private insurance, precisely because they represent a greater risk. Even if risks and premiums were no higher, however, they would still represent a larger proportionate cost to poorer households than more prosperous ones, contrary to the traditional principles of systems of social welfare.

Although it might be argued that the state already redistributes income to the elderly in the form of pensions and that these can be used to cover the costs of caring, pensions are intended both to maintain some continuity of income and living standards when people retire and to ensure that income does not fall below an unacceptable level, rather than to meet the often substantial additional costs involved in the provision of care. In practice, as indicated below, though the general prosperity of those in retirement may have increased in recent years, the level of pensions in relation to earnings from work is still low in many Member States, especially for the most elderly whose need for care is likely to be greatest. As a result, as indicated in Chapter 3 and below, pensioner households in all parts of the Union are more likely to have poverty levels of income than others.

The concern here is to examine the varying approaches to the long-term care needs of the elderly in Member States and the developments which have occurred in recent years. First, however, income levels of pensioners in different age groups are considered in relation to income from employment on the basis of data from the new European Community Household Panel (ECHP).

The level of benefits to old-age pensioners

Comparatively little information has been available in the past on the income received by those in retirement and how it compares with the average earnings of those in work. Historically, retirement has been a major source of low income levels throughout the Union. There is growing evidence, however, if too often piecemeal, that, because of improvements in pension schemes and the increasing ability of people to save for their old age as the income they are able to earn during their working careers has risen, the elderly are becoming wealthier. Although no time series data exist to verify whether this is the case across the Union, the results of the first wave of the ECHP throw light on the relative income of both households in which the people are above pensionable age and of pension recipients.

In the Union as a whole — or, more precisely, the 12 Member States for which data are available — the average benefit received in 1993 by those retired, including any special payments for caring needs and private as well as state pensions, amounted to around 60% of average net earnings of those in employment (see Box). For women, the figure was lower at around 55%, partly reflecting the fact that for some men (and some but fewer women) in a number of countries, the pension received may also include a dependent person's allowance (ie in those — Belgium, Denmark, Spain and Italy (in respect of minimum pensions), for example — where the pension payable to a couple is more than to a single person if one of the couple, usually the wife, has not been in paid employment and, therefore, not accumulated entitlement to an individual pension). The average level for men, however, varied from around 70% or over in Germany, France, Luxembourg and the Netherlands to under 50% in the UK, Denmark, Portugal and Ireland (Graph 78, which shows net income received from all benefits, except family-related ones, by those who said that they were retired; it excludes, however, household benefits, such as housing allowances, which in some countries may be significant and which are included in the analysis in Chapter 3).

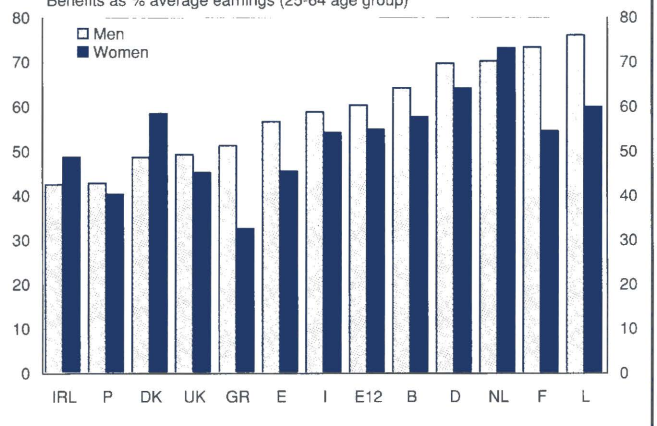
For women, average benefits relative to earnings (in this case, average net earnings of women) were lower than for men in all but three Member States — Denmark, Ireland and the Netherlands — the level varying from over 70% in the Netherlands and almost 65% in Germany to 40% in Portugal and only just over 30% in Greece.

In most Member States, the average benefit tends to decline with age, at least so far as men are concerned. In the Union as a whole, the average for men of 75 and over was some 13% lower than for those aged 65 to 74, and also lower in relation to average earnings of those in work than the figure indicated above (55% instead of 60%) (Graph 79). This reflects both the tendency for pension amounts to have increased over time, partly because of the growth of occupational and private pensions, and the erosion of the real value of the pension received by inflation in a number of countries (though pensions may have kept pace with price inflation, they have failed to match the growth in earnings in many cases). Though varying in extent, the same general pattern is true of all Member States, except Luxembourg. In the Netherlands, Greece and Portugal, the average benefit of those aged 75 and over was over 25% less than for those in the 65 to 74 age group, while in Belgium, Germany and France, it was under 10% less. In consequence, whereas in the latter three countries plus Luxembourg, the average benefit for men of 75 and over was much the same in relation to earnings of those employed as for all men who were retired, in the other countries, it was markedly lower (around 50% of average net earnings in Spain, Italy and the Netherlands, around 40% in the other countries).

For women, however, there is no such general pattern — in 5 Member States, the average benefit of those of 75 and over was higher than for those under 75, in 5 it was lower and in the other two, much the same (Graph 80). Only in Germany and the Netherlands, however, was the level for those over 75 more than 60% of earnings; in Ireland and Portugal, it was only around a third and in Greece under 25%.

These averages conceal wide variations in benefit levels between individuals, which are substantial in a number of Member States, especially in the less prosperous ones. In the

78 Average benefits of men and women aged 65+ in retirement in Member States, 1993



79 Average benefits of men aged 65-74 and 75+ in Member States, 1993

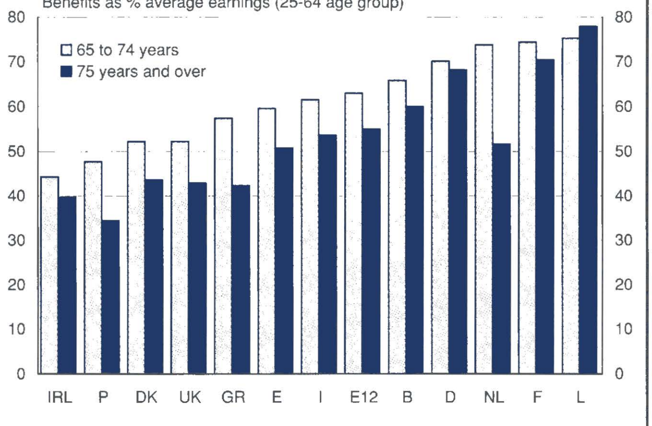


Table 9 — Benefits of men and women aged 65 and over in retirement relative to average earnings by quintile, 1993

% average earnings men/women, 25–64

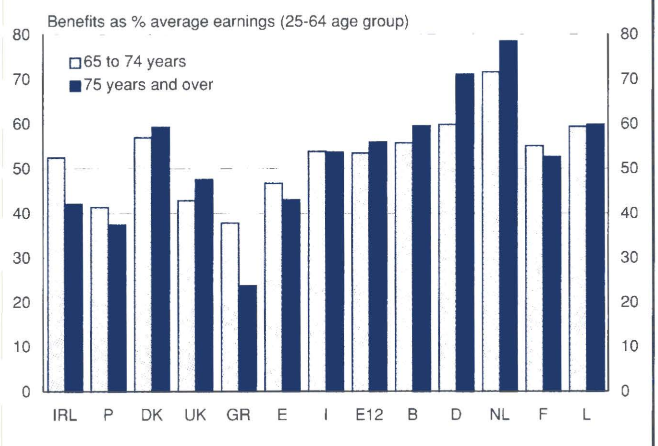
	B	DK	D	GR	E	F	IRL	I	L	NL	P	UK	E12
Men													
Bottom quintile	44.2	32.5	43.0	10.5	36.8	35.0	26.4	31.7	43.6	36.7	19.3	27.8	27.9
2nd quintile	55.0	38.1	57.0	42.0	40.3	52.9	29.8	43.3	58.8	53.2	24.0	35.0	39.1
3rd quintile	64.1	44.4	70.4	54.1	51.8	70.3	40.8	61.6	75.4	65.1	30.5	45.1	50.4
4th quintile	80.3	60.1	88.1	81.7	73.9	96.4	55.6	80.1	97.9	102.1	56.3	67.1	70.8
Mean	64.2	48.6	69.6	51.3	56.6	73.3	42.5	58.8	76.0	70.2	42.7	49.2	60.3
Women													
Bottom quintile	35.3	42.6	30.5	11.5	30.0	20.7	35.0	37.6	31.2	43.6	22.2	26.1	24.9
2nd quintile	52.3	53.2	50.5	11.5	38.5	36.3	37.8	40.8	55.3	58.1	29.3	36.9	41.6
3rd quintile	62.1	57.5	71.1	20.4	41.3	53.8	43.2	47.6	63.3	66.7	33.2	41.7	47.4
4th quintile	76.9	69.6	93.0	50.0	51.1	79.8	64.8	74.4	74.1	82.9	49.6	57.4	65.2
Mean	57.7	58.4	64.1	32.5	45.5	54.6	48.6	54.2	59.9	73.1	40.2	45.1	54.8

Union as whole, 60% of men aged 65 and over in retirement in 1993 received benefits which were 50% or less of average earnings from employment and for 20% the amount received was under 28% of average earnings (Table 9, showing relative benefits of men and women by quintile). At the same time, only 20% received benefits of more than 70% of average earnings.

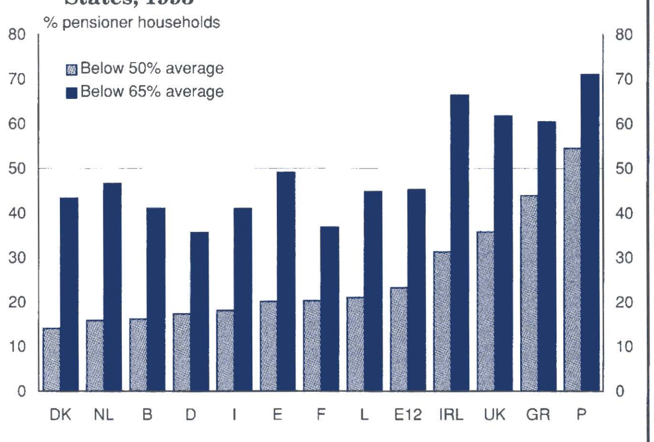
Low benefit levels are particularly evident in Portugal, where only 20% of men were in receipt of payments of more than 57% of average earnings, while 60% had benefit levels of 30% or less of average earnings. Moreover, in Denmark, Ireland and the UK, for 60% for men, benefit levels were under 45% of earnings, while in Greece, where extremely low benefits are most evident, 20% received an amount equivalent to only 10% or less of average earnings. By contrast, in Belgium, Germany and Luxembourg, only 20% or so of men received benefits of under 45% of average earnings, and in France, Luxembourg and the Netherlands, for around 20% of men benefits were similar to average earnings or higher.

Much the same pattern of dispersion of benefit levels is evident for women, though in some Member States, there are significant differences. In Greece, in particular, low benefit levels are even more in evidence for women than for men,

80 Average benefits of women aged 65-74 and 75+ in Member States, 1993



81 Pensioner households with income below 50% and 65% of average household income in Member States, 1993



60% of those aged 65 and over who have retired receiving amounts of only 20% or less of average earnings, while in Denmark, proportionately fewer women than men seem to have low benefit levels, only just over 20% receiving amounts equivalent to 45% of average earnings or less.

In sum, therefore, a significant number of people of 65 and over across the Union receive relatively low levels of benefit, from which they may have to cover the costs of caring.

Pensioner households with low income

The level of benefit which retired individuals receive gives only a very partial insight into problems of low income among the elderly and one which can be misleading. A much more complete picture can be gained by examining income by household, which takes account both of the possibility that people living together each receive a pension, or other benefits, and of income from sources other than benefits, such as interest from savings. It also allows household benefits, such as allowances for rent, to be included in the analysis.

The results indicate that pensioner households are far more likely in most Member States to have low levels of income than other households and that a substantial proportion of them have poverty levels of income as conventionally defined (less than 50% of average income in the country in which they are located).

As noted in Chapter 3, pensioner households, defined as those where the members were all 65 or over, accounted for 22% of all households in the Union in 1993, but for 30% of households with income of under half the national average (income by household is weighted by the number of adults and children living in them — see Chapter 3). Accordingly, just under 24% of households consisting of people of 65 and over had an income of under half the national average, significantly more than the figure of 17% for all households. Moreover, for just over 45% of pensioner households, income was less than 65% of average as compared with only 30% of all households (Graph 81).

The relative number of pensioner households with low levels of income varies markedly across the Union, broadly in line with the variation in average benefits examined above, with the exception of Denmark, where despite relatively low individual benefit levels, a comparatively small proportion of elderly people live in households with poverty levels of income. In Portugal, where a large number of those of 65 and over had low benefit levels, 55% of pensioner households had income of under half the national average and 71% income below 65% of average, while in Greece, where benefit levels were also low for many people, the respective proportions were 44% and 61%. Similarly, in the UK and Ireland, around a third of pensioner households (slightly more in the UK, slightly less in Ireland) had income of under 50% of average and well over 60% — more than in Greece — had income of less than 65% of average. These proportions were, in all cases, much higher than the corresponding figures for all households, though the latter were higher in these four countries than in the rest of the Union (see Chapter 3).

By contrast, a much lower proportion of pensioner households had poverty-levels of income in Member States where a relatively large number of those retired received high benefits, except in Denmark, as noted. In particular, in the Netherlands, Belgium and Germany, only around 17% of pensioner households had income of under half the national average — in Denmark, under 15% — and in France, only 37% had income below 65% of average. Although these proportions were, for the most part, closer to the figures for all households than in the case of the countries examined above, they were, nevertheless, higher. Indeed, in Denmark, which had the lowest proportion of households below half average earnings in the Union (only 8½%), the figure for pensioner households was markedly higher, and some 42% of all households with income below this level were ones where the members were 65 or over.

The evidence, in general, therefore, seems to confirm the findings for individual benefit levels, that a substantial proportion of elderly people in retirement have relatively low levels of income in a number of Member States and that throughout the Union the relative number of pensioner households with low income was greater than for other types of household. Moreover, as indicated in Chapter 2, the tendency across the Union is to reduce state pensions because of the growth in the numbers in retirement, though this may be offset by the increasing importance of occupational and private pensions to supplement the amounts received from the state.

Policy developments across the Union

The response of governments in Member States to the growing demand for long-term care as the number of elderly people increases has taken various forms, according largely to the system already in place for providing support. The main developments are described below country by country, the aim being not to present an exhaustive account of the measures which have been adopted but to indicate the direction of change and the variant approaches to the problem.

The description does not cover the four Southern Member States, largely because the issue is not yet so pressing in these countries, partly reflecting the greater prevalence of the extended family and the tendency for care to be provided from within the home. While social assistance is available for low income households, this tends to be organised on a regional basis and so varies between different areas. Nevertheless, there is some debate in the countries concerned on developing more coherent and extensive systems of support for long-term care. In Italy, in particular, the Onofri Report at the beginning of 1997 recommended that a new fund be established for the provision of long-term care.

The account of developments below is organised by groups of countries with similar features, as follows:

- Germany and Austria, where new social benefits have been introduced in recent years to help cover caring needs;
- Belgium, Luxembourg and France, in which social protection is organised in a similar way and where there are proposals to introduce an allowance for caring;
- Denmark, Finland and Sweden, where social services and support facilities are more extensive than anywhere else in the Union and where there is little distinction between the provision of long-term care and health services, together with the Netherlands, which is similar in the latter respect;
- the UK and Ireland, where there is considerable reliance on informal and voluntary care, where social services locally are underfunded and where financial support is means-tested and available only to those on low incomes.

Germany

The introduction in Germany in 1995 of a new specific function for providing support for the long-term care of the elderly — *Pflegeversicherung* — as part of the social insurance system was an innovation which attracted much attention in other parts of the Union facing similar problems. The motivation was the fact that around a quarter of people over 60 seem to require some kind of assistance in their daily life and a great many of these are in need of social assistance to help cover the costs involved. (Some 70% of those in residential care, for example, require social assistance in the former West Germany and all of those in the former East Germany.)

The scheme introduced is intended to provide only a basic level of income support, priority being given initially to community care, where the need seemed to be greatest. Benefits for care at home became payable in April 1995 and those for residential care (either short or long-term) in July 1996. Since then beneficiaries have been free to choose between the two forms of care, the maximum amount payable being the same in both cases. The scheme is a compulsory part of social insurance for those in work. It is financed from income-based contributions split equally between employers and employees (though the potential effect on labour costs was offset by the withdrawal of one day's holiday each year) and covers around 90% of the population. People are free to take out additional private insurance if they wish and receive a tax incentive to do so. Contributions are intended to finance all social expenditure on care, including investment in support services and, for example, the construction of residential homes.

The amount payable under the scheme is not means-tested, though it varies according to the extent of care required, people being classified to one of three groups — those who need daily help, those who need help three times a day and those who need permanent care. It is also higher when support is provided in kind through the direct provision of services rather than in cash. The scheme covers, in addition, some of the social contributions which informal carers have to pay, as well as equipment which the person in need of care might require, such as a wheel chair.

Austria

In Austria, efforts have been made in recent years to reform the health insurance system, with the particular aim of reducing hospital-based care, which absorbed a major part of the health budget, and increasing the role of community care, which accounted for a minor share and which was generally considered to be underfunded. Responsibility for the latter lies with the regions, or provinces, which up until the early 1990s, were also responsible for financing expenditure, and which differ in terms of the regulations applied to the provision of care and the precise systems in operation. The partial system of allowances, which existed up until 1993 to help those in need of care to meet some of the additional costs involved, was also administered and funded by individual provinces and varied in its application across the country.

In 1993, the Federal Attendance Allowance Act introduced a new allowance, the *Bundespflegegeld*, with guaranteed funding from the Federal government out of general taxation, but still administered by the provinces. This is payable not just to the elderly but to all those over the age of two with disabilities or chronic illnesses, who accordingly require at least 50 hours of attendance or care a month. The amount paid is not means-tested, as it is, for example, in the UK or Ireland, but is based on a medical assessment of the hours of care needed each month. In 1996, the amount was reduced by some 20% in nominal terms and since then it has not been indexed for inflation. (There are 7 levels of payment, at present, ranging from 160 ECU a month for 50–75 hours of care and 275 ECU for 75 to 120 hours to 1,200 ECU for over 180 hours of constant attendance and 1,600 ECU for complete immobility; just over half of all beneficiaries fall into the 75–120 hour category.)

The allowance is intended to cover the additional costs that the person in need of care incurs — for support services, diets, housing and heating, in particular. For those in residential care who are entitled to an allowance, 80% or so of the amount payable goes directly to the care provider (usually the provincial government), while the people themselves receive some 42 ECU a month as 'pocket money' (reduced from 85 ECU in 1996). Other beneficiaries are free to spend the allowance as they choose and, although it can be effectively transformed into direct services if people are not able to organise care for themselves, most recipients use it to pay for informal care provided from within the family.

At present, there is a growing political debate in the context of rising unemployment on whether the payment should be transformed into some kind of system of vouchers, redeemable against the provision of care from outside the family, so creating new employment opportunities in social services.

Belgium

A new old-age insurance system ('autonomy' insurance) is planned in order to increase social protection for the elderly and ensure that they are as independent as possible during the later stages of their life. Support will take the form of a cash allowance intended to cover the non-medical costs arising from the need for care — ie those which are additional to normal living expenses — the amount payable being determined for each individual by a multi-disciplinary team in the light of their degree of dependency and income.

The scheme will replace the present *allowance for assisting older people* and will be financed partly from the present budget for this, partly from the health insurance budget for district nursing, which covers old-age and nursing homes, and partly from new social contributions (though additional 'start-up' funding will be required to create working capital and reserves). Potential problems which might arise concern both the proposed method of funding, in that the transfer of some of the functions and budget from the health insurance programme will not be accompanied by any additional resources, which seem at present to be insufficient to meet needs, and the possible difficulty of distinguishing non-medical caring needs from medical ones.

Luxembourg

In Luxembourg, a draft bill was presented in October 1996 proposing the introduction of 'dependency insurance' as a new aspect of the social protection system, intended to cover the costs of providing the care and assistance required. The new benefit will be financed partly from general taxation (45%) and mainly from compulsory social contributions, levied on those in employment and those receiving insurance benefits (old-age pensions, for example) at a rate of 1% of earnings. It will be payable to the person insured and their families on an unconditional basis (ie it will not be means-tested) in the event of them needing care. The two priority areas of expenditure will be on rehabilitation — ie on attempts to get the person concerned well enough not to need care — and on home support.

France

In France, where no specific scheme exists for providing long-term care to the elderly, there has been much debate in recent years about creating such an arrangement as part of the social insurance system. This has been prompted by the apparent inadequacy of certain services, especially a lack of medical facilities in both residential and community care and the difficulty of many elderly people in need of care to pay for the services they require, which has led to an increase in social assistance as well as greater financial pressure on the families concerned.

A number of proposals have been made to improve the situation. In 1993, it was suggested that a non-means-tested dependency insurance scheme should be established for the elderly, with support taking the form of credits for home-help, informal care and any special equipment required. In 1995, a trial scheme involving increased payments to the elderly in need of care was launched in 12 French regions, payment consisting of the existing means-tested allowance (*allocation compensatrice*), administered on a regional basis and differing in scale across the country, and an additional dependency allowance. The latter was allocated according to income and the degree of dependency, with the family potentially having to pay it back over time. Initial evaluation of the scheme suggested that the allowance was too small to cover the cost of outside help for those in the greatest need of care and was, accordingly, likely to be used to pay for informal care from within the family rather being a means of creating jobs in social services.

From 1997, a specific dependency allowance (*prestation spécifique dépendance*) has become payable on a means-tested basis and increased emphasis has been placed on the role of the family in providing care. While the economy remains depressed and while there is a concern to avoid increases in social contributions, the introduction of a dependency insurance system, with benefits payable as a right, appears to be ruled out.

Denmark

In Denmark, as in the other Nordic countries, no clear distinction is made between medical and non-medical care and there is a more extensive system of publicly-financed support than in most other parts of the Union, with services being provided directly by the state. Finance is from general taxation, though services are administered and organised on a local basis by the municipalities (which are responsible for nursing homes, whereas hospitals are organised at the county level).

In 1988, a programme was launched aimed at increasing the independence of the elderly and improving the quality of services and housing available to them. Following the recognition that those living at home would become more dependent as time passed, increasing numbers of special housing complexes have been built to replace nursing homes while at the same time support services have been developed in place of residential care. This has been accompanied by an increase in financial incentives to municipalities to encourage them to undertake such investment and by the payment of subsidies to private concerns involved in the construction and letting of special housing.

It has also been accompanied by a special programme, aimed at both helping municipalities meet their caring obligations and reducing unemployment through reimbursing 50% of the increase in wage costs involved in providing support services to the elderly if people unemployed are taken on to do this.

Concern at present centres on two issues: first, the overall cost of providing long-term care for the elderly in a context of budget restraint, which has already seen cuts in health expenditure, housing subsidies and home-care services, and how far the state should continue to take full responsibility for this; secondly, the degree of individual choice over the type of care received. On the first issue, public opinion seems to be in favour of extensive state support continuing. On the second, there is growing recognition that the present system, based on the direct provision of care, limits the choice of the person concerned about how they should be cared for and how the transfers they are entitled to are spent (those in residential care, for example, receive only a small part of their pension).

Finland

In Finland, as in Denmark, there is a publicly-funded, universal system of protection, which gives little reason or incentive for private saving or insurance against the risk of needing care. Nor is there much debate about moving to a different kind of system. There has, however, been some concern about the under-provision of community care, which is organised on a regional basis, and about the way that services vary between different parts of the country.

Although the provision of services remains based on need, some means-testing has been introduced for non-essential and non-urgent aspects such as transport. The emphasis of policy is increasingly on community rather than residential care as well as on increasing the extent to which this is targeted on those most in need. Charges for both community and residential care have tended to increase significantly and, as in Denmark, a major part of the personal pension of residents is paid direct to the institution rather than the individual. This has prompted some concern about people being left with too little to meet incidental expenses, as well as about more general issues regarding the quality of personnel, the responsiveness of institutions to individual needs and the lack of choice open to those being cared for, as well as the inadequate availability of services in some areas. The debate, in other words, is focused not so much on financial issues or the role of the state but more on the quality of service and the adequacy of provision.

Sweden

The system of care for the elderly in Sweden is similar to that in Denmark and Finland, with the municipalities being responsible for local support services and residential homes and with funding provided centrally. In recent years, there has been a downsizing of the services available and the support provided, together with increases in direct charges and a tightening of the criteria for eligibility for assistance. In 1996, public pressure led to new funds being made available to municipalities for the provision of care, while, as in Denmark, the opportunity was used to expand resources in a low-cost way by creating jobs for the unemployed in care services, funded from the unemployment insurance funds.

The growing demand for long-term care is being met by a combination of increased taxes and social contributions, greater efforts to improve efficiency and cost effectiveness and the involvement of private insurance schemes to relieve the state of some of the burden of satisfying future needs. As in the other two countries, there has been growing concern about the quality of care as well as about the right of individuals to choose the form of care received.

Netherlands

In the Netherlands, as in other countries, there has been ongoing discussion of the care and housing needs of the elderly, in a context where, historically, policy has concentrated on providing residential care, administered and funded under the *Exceptional medical expenses* scheme. More recently, the trend has been away from institutionalisation towards helping to support care at home, as well as towards changing the nature of residential accommodation, converting old people's homes either into nursing homes or into sheltered housing complexes where the elderly can live independently but within close reach of support.

At the same time, the 1995 reform of the health care system has led to long-term care being more clearly distinguished from basic medical care, but health and social services being made less distinct, the administration being shifted from the health insurance funds to a single authority in each of the 27 regions. This will be responsible for purchasing care on behalf of those in need and for administering both residential facilities and community care, including home-help as well as district nursing (see Chapter 6 for an account of the reform). The cost of care provision is covered by national health insurance (*AWBZ*), with those being cared for being responsible for covering their living expenses.

Although those in need of care have only limited choice over the way that this is provided, a small part of the budget for home care (5%) has been set aside since 1995 for those being cared for to spend as they wish, most,

Long-term care in the UK

A report of an independent inquiry, established by the Rowntree Foundation, into the costs of long-term care for elderly and disabled people, published in 1997, concluded that the provision of care has shifted increasingly from the National Health Service, free at the point of delivery, to means-tested provision organised by local authorities. As a result, a number of people faced 'catastrophic costs' because of the relatively low income plus accumulated savings limit applied to eligibility for free access to services. It also pointed to inadequacies in the provision of care in the community, an aspect examined by the National Association of Citizens Advice Bureaux which reported in the same year. The main finding of the latter was that limits on central government funding to local authorities, in a context where health authorities were accelerating the discharge of elderly and disabled people from hospitals and nursing homes, has led to support for home-care and other community services being rationed. While those affected were usually the ones with lesser needs, the lack of support and preventative services for them made it more likely that they would need residential or hospital care in the future.

in practice, choosing to give this to friends and relatives helping to look after them rather than to professional carers.

UK

In the UK, long-term care of the elderly is provided to a major extent from within the family with support from voluntary organisations. Financial assistance is available both to those receiving care, in the form of an attendance allowance, and to those providing it, in the form of an *Invalid Care Allowance*, introduced as long ago as 1975. Both are non-contributory but strictly means-tested and are payable only in cases where the person being cared for requires attendance for at least 35 hours a week, and, in the case of the *Invalid Care Allowance*, where they are in receipt of the attendance allowance and where the carer earns less than a small amount from employment. Although the amounts involved are relatively small, they are accompanied by entitlement to various benefits in kind, to cover housing costs, local taxes, heating expenses and so on.

Social services and community care are provided by local authorities, but these are increasingly limited because of budget constraints and are targeted ever more narrowly on those most in need. The burden on local authorities, moreover, has increased substantially in recent years with the implementation of the *Care in the community* policy which has been associated with a major shift from residential care to caring for people at home, but without adequate resources being made available to provide sufficient levels of support for those taking on caring responsibilities. At the same time, residential care has become increasingly privatised and fees are covered by the state only if the income plus accumulated savings of those in need is below a certain (relatively low) level (see Box).

While the former Government proposed that people should take out private insurance to cover their potential need for care in old age, a recent Rowntree Commission report has recommended the establishment of a national care insurance scheme and a National Care Council to oversee policy in this area. However, there has as yet been no move by the present Government in this direction.

Ireland

In Ireland, a debate is just beginning on the possibility of including long-term care for the elderly in the social insurance system. At present, the informal caring sector takes a large part of the burden, partly because of an under-provision of resources in community care — funded from general taxation — and a shortage of basic services to support caring at home as well as of more advanced facilities. Although a carer's allowance was introduced in 1990, this is means-tested and conditions for eligibility are very restrictive (being payable only to those living with and caring full-time for someone else in the family).

Residential care is also financed from taxation, though institutions tend to obtain most of the old-age pension paid to residents. Subsidies are available to help cover private or voluntary-sector nursing home fees, but these are limited and eligibility is subject to means-testing and/or the extent of disability. Residents have to pay a third of the costs on average, which gives rise to problems for those with low income in areas where long-term places in publicly-funded homes are limited.

Concluding remarks

The developments summarised above indicate that, while different approaches to the long-term care needs of the elderly are being followed across the Union, there are a number of common aspects. In particular, it seems to be commonly agreed that a primary aim should be to ensure that those in need of care retain as much independence as possible. This means that, so far — and as long — as it is feasible, they should be looked after in their own home, which necessitates the need for support services to facilitate this and to give help to family members where required. Similarly, where this is not possible, sheltered accommodation or special housing complexes should ideally be developed to give people some independence but with immediate access to medical and other kinds of help should they need it.

There also seems to be a widespread recognition that those being cared for should have more say over the form which care takes and over the way that the social transfers effectively allocated to them are spent. This is especially so in countries, such as the Nordic Member States, where social services are well developed and support is organised on a formal basis, giving rise to substantially more jobs than in the rest of the Union. On the other hand, in Austria, where the caring allowance is spent mostly on informal care from within the family, there are proposals to move in the opposite direction. These are echoed in a number of other countries where the employment-creating potential of the development of more formal support arrangements has been highlighted. Budget constraints and a policy emphasis on reducing rather than expanding public expenditure, however, represent a formidable obstacle to this kind of development.

The same budget constraints, allied to a concern to avoid increases in taxes and social contributions, have deterred the development of social insurance benefits for long-term care outside a few Member States and even there have limited the scale of payment (to covering only basic needs in Germany, while it has been reduced significantly in Austria). They have also led to reductions in the provision of social support in the Nordic countries as well as in the UK and Ireland, where help for those in need of care is rationed through means-testing, an approach which seems to be gaining ground in other countries.

Accordingly, as is only to be expected, private arrangements for providing care and for insuring against the future need for care are developing, encouraged in many cases by governments anxious to relieve social protection budgets of the cost involved in state provision. In the same way as means-testing, however, such a policy implies that a disproportionate cost is likely to fall on the poorer members of society, if not the poorest, who are, moreover, most likely to need care.

protection as defined above. Over time, such differences ought to diminish in importance as experience is gained and as national systems of data collection adapt to the new conventions.

Problems of comparability also extend to the functional classification of benefits which is intended to divide spending between the different needs which social protection is aimed at meeting. The broad functions, or areas of need, distinguished in the system are as follows:

Sickness/health care —	Income maintenance and support in cash in connection with physical or mental illness, excluding disability. Health care intended to maintain, restore or improve health irrespective of the origin of the ailment.
Disability —	Income maintenance and support in cash or kind (except health care) in connection with the inability of people with physical or mental disabilities to engage in economic and social activities.
Old age —	Income maintenance and support in cash or kind (except health care) in connection with old age.
Survivors —	Income maintenance and support in cash or kind in connection with the death of a family member.
Family/children —	Support in cash or kind (except health care) in connection with the costs of pregnancy, childbirth and adoption, bringing up children and caring for other family members.
Unemployment —	Income maintenance and support in cash or kind in connection with unemployment.
Housing —	Help towards the cost of housing.
Social exclusion not elsewhere classified —	Benefits in cash or kind (except health care) specifically intended to combat social exclusion where they are not covered by one of the other functions.

Since institutional arrangements for delivering benefits in these areas differ markedly between countries and since a given type of benefit is often aimed at meeting more than one kind of need, it can be difficult for Member States to divide expenditure precisely between these different functions and they may, indeed, lack the detailed information to be able to do so. Early retirement pensions, for example, which may be given in part for labour market reasons and which to this extent ought to be partly classified to unemployment, are an important case in point. In practice, for some Member States, such expenditure is at least partly included under unemployment, in others, not at all, though it is hard to know whether this reflects genuine differences or merely statistical difficulties.

The social exclusion category gives rise to a similar difficulty. Insofar as this is intended to cover expenditure which is not primarily incurred under one of the other heads, the spending included in this function in any Member State might well be affected by practical problems of allocation, though again, it is hard to identify the extent to which this is the case. In addition, expenditure included in the unemployment function should, in principle, encompass the provision of vocational training to those out of work, insofar as this is funded by public authorities. In practice, it is included in some countries but not in others, which is a further source of difficulty in comparing spending between Member States both under this head and in total.

The analysis in Chapter 3 of the present report, on the one hand, aggregates expenditure on old-age and survivors, partly because of the potential difficulties of distinguishing consistently between the two, and, on the other hand, separates expenditure on health care (benefits in kind in the sickness/health care function) from sickness benefits (cash transfers in the sickness/health care function). Because of the comparability problems noted above, however, the analysis of the functional division — the pattern of social protection spending — should be interpreted as being indicative only.

Overall, total expenditure on social protection as defined under the revised classification system is not so different from that defined under the previous system, which formed the basis of the 1995 *Social Protection in Europe* Report. The main change is the reduction from 12 functions to the 8 listed above, together with a more detailed division of outlays by type of expenditure, specifically, whether or not it is subject to means-testing and whether it is takes the form of cash transfers or benefits in kind.

As emphasised in the text, the figures for expenditure are gross of any taxes or social charges levied on transfers, which are important in some countries and which reduce both the value of the benefit to recipients and the effective cost to governments. They also exclude transfers provided through tax concessions, rebates or allowances, which also vary in importance between countries, and to this extent understate the overall financing implications of social protection.

For receipts, the data include contributions imputed to employers as well as actual social contributions. These are intended to reflect the costs to them of providing social benefits to their employees, other than through insurers or through a separate reserve. Since such benefits are included in expenditure, the related need for financing has to be included in receipts.

The main focus of the analysis in the text is on the period 1990 to 1995, for which reasonably consistent data are available for most Member States, though not all — data exist for Denmark only for 1990 (though not for receipts), 1994 and 1995, there are data for Greece only for total expenditure in 1993 to 1995, as noted above, and data for Sweden only for the same years.

Germany

Data in this report for Germany include the former East German Länder throughout. Since consolidated figures exist only from 1991, the figures for 1990 have been estimated from the data for the former West Germany (specifically, the change for West Germany between 1990 and 1991 is applied to the 1991 figure for total Germany to derive an estimate for 1990 which is comparable to that for later years). This is also the case in respect of LFS data.

UK

ESSPROS data for the UK are on a financial year basis (ie April to March) rather than a calendar one as for other countries. Figures for GDP and for the relevant price indices have been adjusted approximately to the same basis when calculating expenditure relative to GDP and changes in real terms.

European Union

Figures for the European Union relate to total expenditure in the Member States indicated relative to total GDP in these countries or to population or are weighted averages of changes in Member States (where the weights are expenditure in the base year).

GDP

The GDP figures used in the report with which the expenditure data are compared are the latest available as of March 1998.

PPS

Expenditure is expressed in terms of purchasing power standards (PPS), which takes account of differences in price levels between Member States (specifically of those of consumer goods and services), when making comparisons of the level of spending in different countries. For the Union as a whole, figures in terms of PPS are the same as ECU figures.

Country notes

Denmark: No comparable data are available for receipts before 1994. Incomplete data exist to divide contributions of protected persons between employees, the self-employed and pensioners and other benefit recipients. They are allocated here wholly to employees, who are by far the largest contributors.

Germany: Unemployment benefits include some wage subsidies paid to employers to encourage the employment of certain groups at risk on the labour market (amounting to around 16% of total spending on this item in 1995). The new long-term care benefit introduced in 1995 is included largely in old age (accounting for around 1% of spending on this item) and partly in disability (accounting for just over 2% of spending).

Italy: Old-age pensions include early retirement benefits paid to those unable to find employment. Unemployment benefits include spending under the CIG (*Cassa Integrazione Guadagni*) paid to those on lay-off (amounting to some 28% of expenditure on this item in 1995).

Luxembourg: Data by function are available only for total expenditure on each — ie there is no breakdown between cash benefits and benefits in kind or between means-tested and non-means-tested benefits.

Austria: Unemployment benefits include some subsidies to employers (though these accounted for under 1% of spending on this item).

Portugal: Unemployment benefits include support for employment creation in the independent sector (accounting for under 2% of spending). 'Other receipts' include proceeds from asset transactions which cannot be separately distinguished.

UK: Because data only for total expenditure by function are available for 1995, the detailed breakdown of spending within function and the cost of administration are estimated from the 1994 figures. Old-age pensions, as noted above, exclude Appropriate (or approved) Personal Pensions, which fall within the definition of social protection. Means-tested benefits in kind in the disability, old-age and family functions include some benefits not subject to means-testing.

For more details on the ESSPROS data, see *ESSPROS Manual 1996*, Eurostat, 1996 and *Social protection expenditure and receipts, 1980–1995*, Eurostat, 1998 (forthcoming)

European Community Household Panel

The analysis of social transfers to households in Chapter 3, of unemployment benefits relative to wages in Chapter 4 and of transfers to people retired in Chapter 7 is based on the first wave of the new European Community Household Panel (ECHP). This is an annual survey of a representative panel of households and the individuals who live in them, covering a wide range of topics, including living conditions, employment status, health, education and, most importantly for the present report, of income and the various sources from which it comes. The aim is to interview the same households and individuals over a number of consecutive years so that changes in their circumstances over time can be monitored. The survey is based on a harmonised questionnaire, drawn up by Eurostat, and subsequently adapted by the national agencies responsible for collecting data in each of the countries to take account of their own institutional features.

The first wave of the ECHP, which at the time of preparation of this report is the only one for which data are as yet available, was conducted in 1994 in the 12 Member States which then comprised the Union and covered some 60,500 households in total (about 170,000 individuals) and 5,000 or more in most Member States. The sample size, however, varies between countries in relation to population. It is relatively small for Germany, where only 5,000 households were covered because of legal restrictions, and the UK, where under 6,000 households were covered, but relatively large for Greece, where the number was much the same as in the UK, and Spain, where over 7,000 households were included. The sample in all countries should be large enough to give reasonably reliable results for the issues examined here. Where the number of observations size falls below a minimum level (taken as 25 individuals or households), the country concerned is excluded from the analysis.

Data for the second and third waves should become available during 1998, the former (for 1995) including Austria and the latter (for 1996) including Finland. These data will enable the results of the first wave to be more thoroughly checked and verified. As a result, they are liable to change as this exercise is undertaken, which could affect the findings presented here.

The data for social transfers analysed in the text relate to cash receipts by individuals and households net of any taxes or social charges paid on these. For France, however, the figures are gross of direct taxes which are not deducted at source and to this extent are not strictly comparable with those for other countries. In principle, all transfers which provide income support should be included, except study grants and transfers between households. (For a detailed description of the ECHP methodology, see *The European Community Household Panel (ECHP): Volume 1 — Survey methodology and Implementation*, Eurostat, Luxembourg, 1996.)

European Union

Figures for the European Union, as for the ESSPROS data, are weighted averages of those for the Member States. Accordingly, figures in Chapter 3 for the proportion of households with an income below a given percentage of the average relate to the relative number in the Union with income below this percentage of the average in the Member State in which they live, rather than to the proportion of households with income below a given percentage of the Union average.

European Community Labour Force Survey

The LFS, which is used in Chapter 1 and Chapter 5 of the report, is also an annual survey of households, though the sample size is considerably larger than the ECHP. Conducted each year since 1983 and covering all 15 Member States, it is focused more narrowly than the ECHP on employment issues and is similarly based on a common set of questions and definitions, so abstracting from national differences in methods of classification and institutional arrangements.

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