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COMMUNICATION FROM THE COMMISSION

**MODERNISING AND IMPROVING SOCIAL PROTECTION
IN THE EUROPEAN UNION**

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EXECUTIVE SUMMARY

Publicly funded social protection systems provide the bulk of expenditure on social support, health care and pensions in the Member States of the European Union. They have played a fundamental role in ensuring income redistribution and cohesion, and in maintaining political stability and economic progress over the life of the Union.

These systems now account for 28 per cent of total EU GDP, although that proportion varies between Member States - from 16 to 35 per cent - depending on differences in levels of provision and differences in the balance of public and private funding.

The objectives and the financial and operational structures of most systems were established decades ago. While the basic needs to which they respond remain, the economic and social conditions under which they operate have changed, and will continue to do so. In order to ensure their continued effectiveness, and in order to meet evolving needs, there is an urgent need for modernisation. In particular, social protection systems need to be adapted to:

- the changing nature of work, where a new interplay is called for between policies designed to improve flexibility and those designed to provide security;
- change in the gender balance in working life, where equal opportunities bring new issues and requirements in terms of social protection;
- the ageing of the population in Europe, where the rapid growth of the dependent population is creating new needs as well as forcing the pace of pension reform;
- the need to reform the co-ordination of national social security schemes for people moving within the EU.

To support the Member States in meeting these challenges, the Commission presented, at the end of 1995, a 'Framework for a European Debate on the Future of Social Protection' that triggered a lively and interactive discussion. It is now time to take stock. This Communication has a dual purpose:

- to indicate the routes along which modernisation can be pursued
- to present some specific proposals for European level support.

This approach is built on the common understanding that:

- Each Member State is responsible for the organisation and financing of its own social protection system.
- The EU is responsible for the co-ordination of national social security schemes in cases where citizens exercise their rights of free movement within the Union.
- The EU also serves as a forum for promoting better mutual understanding of long-term perspectives, and for identifying common challenges facing Member States.

In the light of this, the Commission proposes the following agenda of issues for further analysis, debate and action:

- 1. Social protection as a productive factor:** Building on the discussions which took place at the Dutch Presidency Conference on «Social Policy and Economic Performance» held in January 1997, the Commission will study during 1997 the overall costs and benefits of social protection systems - in particular, their impact on social cohesion, political stability and economic progress.
- 2. More employment-friendly social protection systems:** As mandated by the Dublin European Council, the Commission will, in its contribution to the 1997 Joint Employment Report, focus on *how social protection reforms and taxation can be developed as an integral part of an active employment policy*. This will be based on the examination of best practices in the field of active policies.

The Commission will examine *how reactive unemployment insurance can be turned into a proactive employability insurance*.

The Commission will deepen the analysis of measures *taken to reduce non-wage labour costs* as a contribution to the interim report to be presented at the Amsterdam European Council in June 1997 and to the Joint Employment Report to be prepared for the Luxembourg European Council in December 1997. The effect of taxation on employment will also be an important part of the discussion in the new *Taxation Policy Group* as endorsed by the Dublin European Council.

The Commission will present the potential and problems of a *gradual transition to retirement* in the Employment in Europe report, to be published in September 1997 and will consider appropriate follow-up.

In the first half of 1997, the Commission will present a Communication on *the promotion of social inclusion* and, in the second half of 1997, a report assessing the mechanisms of guaranteed minimum income schemes in the social protection systems of the Member States.

- 3. Adapting social protection to the demographic ageing of European societies:** The ageing of the population in the Member States is putting pension systems under considerable pressure. The Commission will develop *methods for forecasting pension expenditure*, and assess the elements of reform which seem to be most adapted to ensuring the *sustainability of public pension schemes* while preserving their core aspects of solidarity.

In the first half of 1997, the Commission will also issue a Green Paper on *supplementary pensions*, aimed at identifying the main elements of a *framework at European level* in order to provide a secure environment for supplementary pension schemes.

In order to *meet the long term needs of dependent older people*, Member States are undertaking a number of reforms. The Commission will study ongoing reforms and provide the Member States with an overview.

In order to *improve the efficiency and cost effectiveness of health systems*, the Commission will, in 1997, carry out an assessment of the potential impact of prevention on the reduction of health care costs and clarify to what extent and under what conditions, introducing market forces within health care systems can help save costs while fostering a better quality of services and ensuring access for all to health care.

- 4. Adapting social protection to the new gender balance:** The changing gender balance requires both new arrangements for reconciling working and family life, and new initiatives to strengthen individual rights. At the end of 1997, the Commission will present initiatives aimed at *setting higher standards for the care of children and other dependants*. The 1997 Annual Report on Equal Opportunities will *assess the attempts made by the Member States to make progress towards individualisation* without jeopardising the economic situation of women.
- 5. Improving social protection for people moving within the Union:** The Commission will develop a strategy to *reform and simplify the co-ordination of social protection for migrant workers* and to find specific solutions to cope with the cross-border problems in relation to occupational schemes, including, as a first step, during 1997, a proposal for a directive tackling some of these problems.

The Commission invites all **Member States and the European institutions** to engage in a continuing dialogue on strategies for the modernisation of social protection systems, as presented in this Communication. The presentation of the Joint Employment Report for the Luxembourg European Council in December 1997 will offer an appropriate opportunity to scrutinise this strategy.

The Commission also invites **the social partners**, at all appropriate levels, to contribute to this work. The Social Dialogue Committee and the Standing Committee for Employment are invited to play a leading role. The Commission intends to put social protection reform at the top of the agenda for the civil dialogue at the **1998 European Social Policy Forum**, which will involve the Member States, the social partners, NGOs, as well as the European institutions.

Finally, the *Social Protection in Europe* report, to be published at the end of 1997, will bring together more evidence and analysis on recent developments in Member States, as a contribution to the process of joint reflection.

1. A EUROPEAN DEBATE ABOUT THE FUTURE OF SOCIAL PROTECTION

Maintaining a high level of employment and social protection is one of the Community's fundamental objectives and is explicitly included in the tasks listed in Article 2 of the Treaty on European Union. Social protection represents a fundamental component and a distinguishing feature of the European model of society.

The Council adopted in July 1992 a Recommendation on the convergence of social protection objectives and policies¹. The aim of this convergence strategy was to fix common objectives to guide Member States' policies in order to permit the co-existence of different national social protection systems and to enable them to progress in harmony towards the fundamental objectives of the Community. The strategy of bringing about a convergence of policies while respecting the autonomy of systems is a direct application of the principle of subsidiarity.

Each Member State is responsible for the organisation and financing of its own social protection system. However, given the common challenges facing Member States in this area, there is considerable value in discussing these issues at European level. Throughout the European Union, significant reforms of social protection systems are now under consideration and, in a number of cases, are being introduced in response to rapidly changing social and economic conditions².

In the light of this, the Commission presented at the end of 1995 a "Framework for a European Debate on the Future of Social Protection"³. The Commission proposed that the Community institutions and the Member States should examine jointly the measures to be taken in order to make social protection more employment-friendly and more efficient. The social partners and all concerned have been called upon to make their contributions. The European Parliament and the Economic and Social Committee have also been associated in this reflection and delivered opinions. The Confidence Pact for Employment has highlighted the importance of this debate⁴.

1.1 The contributions to the debate

The Framework for Debate⁵ triggered an extremely lively and interactive discussion throughout 1996 in the form of written exchanges, conferences, ad hoc meetings with scientific experts and policy-makers. A summary of the contributions from Member States, the European institutions and the social partners is being published separately as a Commission services working document. There is much common ground in these reactions:

- The European social model is valued and should be consolidated. This model is based both on common values and the understanding that social policy and economic performance are not contradictory but mutually reinforcing. Highly developed social protection systems are a major component of this social model.
- To preserve social protection implies adapting European systems in their various forms, since the context in which they were established has changed. The challenge is to align social protection to the new situation without abandoning its core values of solidarity and cohesion.
- This task is complex and the means to achieve it are uncertain. Each Member State has to find solutions that are adapted to its own particular system. Member States should continue to pursue the convergence strategy as outlined in the 1992 Council Recommendation.
- The means of adapting social protection systems have to be in line with the process of European integration, and in particular the single market, moves towards EMU and progress towards European citizenship.
- The ability to learn from each other and adapt quickly is a key factor for success. The European Union should act as a catalyst to enable Member States to learn from one another's experience and adapt to changed circumstances.

¹ Council Recommendation 92/442/EEC of 27 July 1992 on the convergence of social protection objectives and policies, OJ L 245 of 26 August 1992.

² See reports "Social protection in Europe - 1993" (COM(93) 531) and "Social Protection in Europe - 1995" (COM(95) 457).

³ Communication from the Commission COM(95) 466 of 31 October 1995 "The Future of Social Protection: A Framework for a European Debate".

⁴ Action for Employment in Europe: a Confidence Pact, SEC(96)1093 of 6.5.1996, in particular points 3.11. and 3.16.

⁵ In November 1996, the French delegation submitted to the Council a specific statement in favour of this initiative, as a follow-up of the Turin European Council and the French memorandum on the European social model.

Drawing on the results of this joint reflection process, the Commission undertook to take stock of the reactions to the debate it had launched and to propose appropriate follow-up. The purpose of this communication is twofold:

- to map out some avenues for improving European social protection systems on the basis of the contributions to this debate and identify key actions in each field;
- to present some proposals to involve all concerned in this adaptation process.

1.2 The challenge: The need to modernise and improve European social protection systems

Social protection expenditure now accounts for 28 per cent of the European Union's GDP, with national variations that range from 16 to 35 per cent. It plays a fundamental role in income redistribution and social cohesion, political stability and economic progress. The more working life becomes flexible, the more citizens will demand security from their social protection systems. Good social protection and successful business are therefore mutually supporting.

This view on social protection is underpinned by detailed international comparison, suggesting that, when account is taken of private as well as public spending, total household expenditure on social protection, health care and pensions is at relatively similar levels across a range of developed, industrialised countries⁶. Moreover, Member States with a strong safety net often perform better in terms of GDP per capita or external balance than Member States with a weaker safety net. On the other hand, only countries with a sound economy are able to maintain a high level of social protection. For this reason, the completion and reinforcement of the European single market will become increasingly important.

It is important to realise that the reasons for a reform of social protection systems is not competition from third countries. Free trade and globalisation should not be seen as a threat to the European social model.

The reasons for a reform are internal. The real threat against the European social model would be our inability to cope with the existing pro-

blems. First of all, there is an urgent need to consolidate public finances in most Member States in order to avoid growing deficits and heavy debt services in the future, crowding out expenditure on social protection. This is not in contradiction with a high degree of social protection nor does it dismantle the principle of solidarity. On the contrary, it strengthens solidarity between different generations, since it reduces the burden on future generations.

Secondly, the system needs to be reformed in order to promote economic and social integration. One key function of social protection systems is to provide the categories of people who cannot work with some income security. However, this has simultaneously tended to deter from economic integration. Social protection systems have been both a success, in terms of alleviating poverty, and a failure, in terms of promoting full integration within society.

The magnitude of transfers necessary to pay income compensation for people out of work is growing fast and leads to higher levies on workers' income while the people concerned would prefer to be offered new opportunities to take an active part in economic life.

These problems - big public deficits and the lack of success in social integration - are the real threat to the European social model. Their seriousness can, to a large extent, be explained by the changes in the basic conditions for social protection. Four dominant factors underpin the reform of social protection systems: the changing nature of work, the ageing of the European population, the new gender balance and the need to reform the coordination of national social security schemes for people moving within the EU.

1.2.1 The changing nature of work

The patterns of working life on which income maintenance programmes were built are undergoing fundamental change. New jobs are emerging in the service sector, while jobs in manufacturing industry are decreasing. Skill structures are also changing: we are moving from simple, low-skilled jobs to jobs demanding new, broader and higher skills. The nature of employment is changing: there are more part-time and temporary jobs than ever before. Finally, our working life has become shorter: we spend more time in education and training and start working later, but we leave working life earlier and the average actual pension age is below 60.

⁶ See for instance G. Esping-Andersen: "The Double Problem of Co-ordination in Contemporary Welfare States", paper prepared for the Conference on Social Policy and Economic Performance, Amsterdam, 23-25 January 1997.

⁷ These changes are analysed in the White Paper on Education and Training: «Teaching and Learning: towards a Learning Society». COM (95) 590, which developed the concept of life-long learning, which was equally the theme of the European Year of 1996. These changes are also highlighted in the Green Paper "Living and Working in the Information Society: People First." COM (96)389. Bulletin of the European Union - Supplement 3/96. Furthermore, the Commission is preparing a Green Paper on "Partnership for a New Organisation of Work" to be published in 1997.

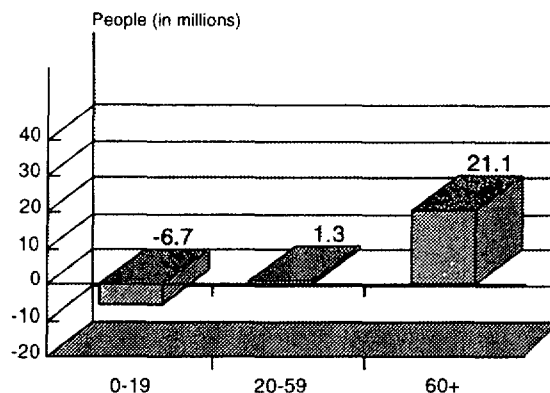
New forms of work organisation are emerging. The 20th century linear career concept will gradually be replaced by a new pattern of varied and variable working life. This implies that, at any given moment, an individual could have several paid activities in progress. Most workers will experience non-working spells during their working life. These will be part of a regular transition from one activity to the other, during which they will adapt their skills or prepare for a new job⁷.

The main lesson from the last 20 years is that income maintenance programmes will not provide adequate security. The huge resources in the benefit systems need to be made more employment oriented. Unemployment benefit schemes must become more effective: increasing *incentives* for the unemployed to look for a job (see 2.2.1) by giving them *opportunities* to upgrade their skills, so as to create progressively a real *employability insurance* instead of a simple unemployment compensation (see 2.2.2). As far as possible, the financing structures of social protection systems should be reformed to allow for *efficient reductions of non-wage labour costs*, especially with respect to low wages (see 2.2.3). A *gradual and flexible transition to retirement* needs to be fostered in order to maintain opportunities for older workers to stay in the labour market (see 2.2.4). At the same time, the role of social protection in promoting social cohesion must be maintained, and Member States are also looking at ways of *integrating everyone fully into society*, including those categories threatened by exclusion (see 2.2.5).

1.2.2 The ageing of the population in Europe

Social protection is also confronted with the challenge of ageing European societies. Between 1995 and 2025, the number of people aged 60 and over, which amounted to 77 million in 1995, will increase by at least 29 million and at most, 44 million. The proportion of older people in the total population will rise from 21 to approximately 30%. The transfers from workers to pensioners through state pension schemes are running at such a level that they are in danger of becoming unsustainable. A number of Member States have begun to initiate *reforms of their pension schemes* (see 2.3.1 and 2.3.2). The ever-growing numbers of very old persons will lead to a rising demand for health care and social services, and Member States will find it difficult to finance increasing health care expenditure. *The search for efficiency in health care systems will become a priority* (see 2.3.4). At the same time, *the care needs of dependent older people* (see 2.3.3) are growing and lead to a new kind of demand on social protection systems, the satisfaction of which has a great employment potential. The challenge is to reconcile the satisfaction of these new care needs with the imperative of containing the relevant care costs.

Population growth between 1995 and 2015 for three age groups European Union (15)

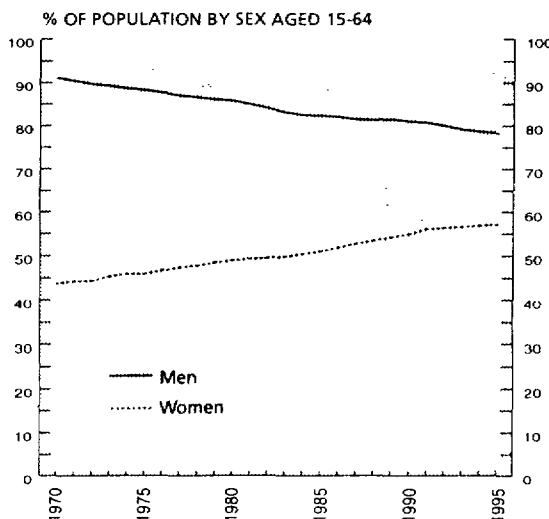


Source: EUROSTAT

1.2.3 The new gender balance

The move towards equal opportunities for women and men has a strong impact on working life and on society as a whole. Women's employment has increased in the Union from 46 to 61 million over the last 20 years, while men's employment has remained remarkably stable (86 million). The trend of increased female participation in employment will continue during the years to come and will make a valuable contribution to countering an impact of the ageing workforce.

Activity rates of men and women in the Union, 1970 to 1995 European Union (15)



Source: EUROSTAT

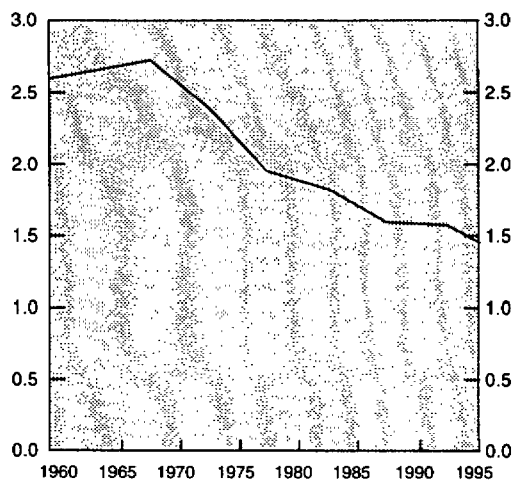
The new gender balance renders the traditional concept of social protection, based on a family in

which the husband is the breadwinner while the wife has no paid work, outdated. There is a conflict between this new balance and the traditional family policy that expects women to take the whole responsibility for housework and child and elder care at home.

The low and falling birth rates in many Member States are strong signals of the need to rethink social protection systems. The challenge for social protection is not only to achieve equal treatment for women and men, but also to find ways of individualising rights without penalising women who have not taken up paid employment in order to look after their families, as well as new arrangements to facilitate care for children and for older people (see 2.4).

Co-ordination is a dynamic process reflecting the evolution of the national schemes of social protection and changing requirements. There is now a need to simplify and reform the co-ordination system to adapt it to new needs derived from new forms of social protection and patterns of migration. Migration consists increasingly of highly skilled workers¹⁰, for whom supplementary schemes of social protection, lacking any co-ordination at European level, are of particular importance (see 2.5).

**Total fertility rate, 1960 - 1995
European Union (15)**



Source: EUROSTAT

1.2.4 The need to reform the co-ordination of national social security schemes

Since 1959⁸, the Union has had a European system for co-ordinating the social security schemes of Member States which protects the rights of people moving within the Union. This means that the social protection of a considerable number of people depends, wholly or partially, on a well functioning co-ordination system⁹.

⁸ Regulations 3 & 4 co-ordinating the social security schemes of the then six Member States, came into force on 1 January 1959. These were replaced on 1 October 1972 by Regulations 1408/71 and 574/72 which are still in force and have since been amended many times. These Regulations have been updated in OJ L28 of 30 January 1997.

⁹ In fact, it determines the social security rights not only for the 2.8 million EU nationals who are at present working in another Member State but also for the millions of European citizens who have in the past, during a period of their career, been working in more than one Member State, or who will do so in the future. The successive enlargements of the Union have increased these numbers considerably and so will any future enlargement (EUROSTAT, Labour Force Survey, 1995).

¹⁰ "Social Security in Europe - Equality between nationals and non-nationals" First European Conference on social security for migrant workers, Oporto, November 1994.

2 THE KEY ISSUES FOR MODERNISATION

2.1 Social protection as a productive factor

The capacity to create jobs for an increasing part of the working population, thereby reducing the dependency ratio, is of fundamental importance for the sustainability of the social protection systems. The creation of jobs and the fight against unemployment is the highest priority of the European Union, as recently emphasised by the Dublin European Council.

The reforms of social protection systems have to be seen in the context of the European employment strategy. The "Broad Economic Policy Guidelines", agreed at the Florence European Council, call for a restructuring of public expenditure in order to make more room for expenditure that can promote employment, including a redistribution from passive to active labour market policies and investment in human resources. A central question arising from the efforts to modernise social protection systems is how to combine obligations and opportunities. More opportunities for individuals to get into or go back to work is a prerequisite for all the measures that put more responsibility on the individual through cuts in social security provisions.

The links between social policy and economic performance have recently been highlighted by the Dutch Presidency at a conference in Amsterdam¹¹. The Commission has gathered information and initiated further studies on the links between social and economic policies. The ongoing work will be brought together in order to stimulate the debate on the mutually reinforcing effects of good social and economic policies.

Objective: Increase awareness of social policy as a productive factor.

Key action: Building on the discussions which took place at the Dutch Presidency Conference on «Social Policy and Economic Performance», the Commission will study during 1997 the overall costs and benefits of social protection systems - in particular, their impact on social cohesion, political stability and economic progress.

2.2 Making social protection more employment-friendly

Today, employment is the first priority and the greatest challenge for the European Union. Building on the Confidence Pact for Employment, and particularly the plea to speed up the reform of employment systems, the 'Dublin Declaration on Employment' adopted at the European Council on 13-14 December 1996 stressed the need for taxation and social protection systems to be more employment-friendly. Furthermore, the Council Resolution of 2 December 1996 on the role of social protection systems in the fight against unemployment¹² specified the way this could be achieved and urged the Commission and the Member States, working in partnership, to strengthen the exchange of information and experience and to deepen the level of joint reflection among Member States on techniques and policies aimed at making social protection more conducive to employment.

It is becoming increasingly clear that *as the nature of work changes, the span of social protection systems must provide more stability and security*. In tomorrow's working world, the balance between flexibility and security must offer recognition and regularisation of new forms of employment relationships. However, it must also offer the security which can result from greater influence over one's work and from having the scope and opportunity to enhance skills and employability.

In order to make social protection more employment-friendly, the following issues should be addressed:

2.2.1 Making tax and social benefit systems more employment-friendly

Taxation and social protection systems need to be made more employment-friendly, by ensuring that they provide clear incentives for job-seekers to take jobs or participate in other employment enhancing activities, while still providing a safety net for the jobless. Improving the articulation between tax and social benefit systems is therefore essential. Dependency on social protection is likely to grow for as long as the net gain expected from return to work is small.

¹¹ Dutch Presidency Conference "Social policy and Economic Performance: employment, activating the welfare state and economic competitiveness" - Amsterdam 23-25 January 1997.

¹² Resolution of the Council and of the representatives of the governments of the Member States, meeting within the Council of 2 December 1996, on the role of social protection systems in the fight against unemployment, OJ C386 of 20 December 1996.

It may occur that an unemployed person gets a disposable income from benefits which is higher than the one he/she could expect when back in work. Although administrative controls and social pressures may lead people to look actively for a job despite high replacement rates, in the long run such a situation is not conducive to employment. Financial incentives are necessary to reinforce work incentives.

Those facing the greatest disincentive effects are those caught in the unemployment trap: loss of benefits, in conjunction with the impact of taxation, can wipe out any advantage expected from bringing an earned income into a family. Benefit recipients are then truly caught in a trap, from which they have no economic motivation to escape.

In particular, social protection should seek to be as neutral as possible in relation to any second paid activity within a couple, and even encourage it. It is becoming rare for social protection benefits - especially family benefits - to be granted on condition that one family member does not have an earned income. Nevertheless, in certain Member States, additional benefits still exist - especially additional unemployment benefits - which are granted only if the unemployed person lives with a partner who has no paid activity. The disincentive effect of these measures is clear.

A further problem is the setting of income ceilings to qualify for benefit. All Member States, with the exception of Spain, pay family allowances to all families, although Germany, Italy and Greece reduce the amount when family income exceeds a certain sum. Where other kinds of family and housing benefits exist, however, they are usually means-tested. It is important in this situation to avoid the poverty trap. This danger can be avoided in two ways: by only partly reducing benefits when household income increases or by introducing a specific, higher income ceiling if two wages are coming into the household. In most Member States, no special provision has been introduced to deal with this problem.

Making social protection more employment-friendly could also take the form of indirect, non-wage income support. The failure of many previous programmes to provide incentives to the long-term dependent, especially women with care responsibilities, was in part a consequence of a failure to compensate sufficiently for the difficulties that the most vulnerable often face in combining family responsibilities and work. The particular vulnerability of single-

parent households or households with only one low income is to a considerable extent due to an inability to combine work and care. Therefore, indirect income support through public or subsidised child care provision can influence labour supply significantly.

Objective: Make social protection more employment-friendly by improving the articulation between tax and benefit systems with a view to increasing employment incentives.

Key action: The Commission will assess, in line with the Conclusions of the Dublin European Council, whether recent changes in policies and systems have strengthened incentives for job seekers to take up work and will identify the obstacles to achieving these objectives.

2.2.2 Turning unemployment insurance into an employability insurance

Incentives to look for employment are necessary. However, incentives need to be boosted by offering better opportunities to find jobs. In the Union as a whole, only 7% of the unemployed are currently offered the possibility of retraining. The vast majority is expected to find a new job in a more knowledge-based economy with often outdated skills.

Most unemployment schemes were designed originally to provide a replacement income for people who found themselves temporarily out of work but expected to find work again soon. In most cases, this new job would require skills similar or identical to those needed for the previous one. Today, however, with the labour market rapidly evolving and responding to changing needs and demands and becoming increasingly skills-based, it has become essential that those seeking employment are prepared to acquire new and different skills. Life-long learning has become an integral part of a full and successful participation in the labour market. Some of the unemployed, in addition to financial support, now require tailored measures and programmes to help them to improve and acquire work skills, training or increase their employability if they are to stand a realistic chance of finding new employment.

Furthermore, figures show that the longer those out of work remain in unemployment the greater their difficulty in regaining a foothold in the labour market. Financial constraints have led a

number of Member States to reduce the average duration of unemployment insurance benefits by linking this duration to previous employment records. A growing number of unemployed people find themselves caught in a process which, as their rights to unemployment insurance are exhausted, can lead to eventual withdrawal from the labour market and an erosion of their work skills. The combined effect of unemployment insurance schemes, which pay benefits for a limited period, and assistance schemes, whether for unemployment or as part of a minimum income guarantee, can be inappropriate to current labour market conditions.

The task, therefore is to provide measures which help the unemployed to acquire new skills and upgrade existing ones, within a framework of social protection that prevents a drift into poverty and exclusion from the labour market and society in general. More attention must be given to a review of unemployment benefit schemes aimed at seeking to assist and guide the unemployed from unemployment through the acquisition of skills and qualifications to enter and re-enter the labour market. Social protection should support reforms aimed at improving the provision of training and general education. A number of Member States have undertaken reforms in their unemployment benefit schemes, with the aim of providing active support to the unemployed at an early stage in the unemployment spell, and to remove disincentives to active job search. The balance must be shifted from passive to active policies that involve participation in training and education and assisting in the finance of schemes to provide work experience.

Objective: Make social protection more employment-friendly by developing unemployment compensation schemes into employability insurance, in line with the move towards life-long learning.

Key action: The Commission will examine the changes in the existing structure and organisation of unemployment compensation schemes necessary to implement the agreed restructuring from passive to active policies.

2.2.3 The funding arrangements for social protection need to be thought afresh

The fight against unemployment is not just about increasing incentives and opportunities for the unemployed to get a job. Arrangements for funding social protection also affect employment - especially the employment of low-skilled workers - through their impact on total labour costs.

The 1993 White Paper on Growth, Competitiveness and Employment¹³ recommended a reduction in non-wage labour costs, ranging from 1 to 2% of GDP for the EU as a whole. This recommendation was further emphasised in the Essen European Council in 1994, where one of the five priorities in fighting against unemployment was identified as the reduction in non-wage labour costs, in particular targeted at unqualified employees. This reduction has not yet been fully achieved. The main reason is the difficulty experienced by Member States in finding suitable and sufficient budgetary compensation to offset the revenue loss.

The long-term trends in taxation have been unfavourable to labour. Between 1980 and 1994, the implicit tax rate on employed labour increased steadily from 34.7% to 40.5% on average in the Member States. Over the same period the tax rate decreased from 44.1% to 35.2% for other factors of production (capital, self-employed labour, energy, natural resources).

Several Member States have introduced various measures to reduce non-wage labour costs. Some studies have shown that they have not led to significant effects on overall employment levels because they trigger substitution effects between subsidised and non-subsidised labour and dead-weight losses¹⁴. At the same time, these studies show that the positive effects will be greater if measures are carefully designed and linked to job creation. Provided these specific reductions of non-wage labour costs are stable enough over time, new job opportunities can be offered to those categories which face the biggest difficulties in integrating into the labour market. In general, a clear signal should be given that the long term trend to increasing taxes on labour will be reversed.

The key gap to narrow is that between, on the one hand, total salary cost and, on the other, net take-home pay for low-skilled workers. There has been little progress over recent years in this respect. There are various reasons for this impasse. It is

13 "Growth, Competitiveness and Employment: A White Paper", COM(93)700, December 1993.

14 See for instance "L'allègement des charges sociales sur les bas salaires", rapport au premier ministre, Conseil supérieur de l'emploi, des revenus et des coûts, Paris, June 1996 and "Labour cost, Wages, and Employment in the EU", note presented to the Economic Policy Committee, September 1996

often difficult to reconcile changing the funding of social protection with preservation of people's rights, especially where benefits are in replacement of salary. There is, however, some room for manoeuvre in certain countries: shifting taxation from labour to other production factors can enable a restructuring of the non-wage labour costs, in order to reduce the burden on low wages. The White Paper on "Growth, Competitiveness and Employment" has already singled out environmental and energy taxes as one of the ways in which the compensation revenues can be levied so as to permit the reduction of taxes on labour.

To achieve that transformation, closer co-operation between Member States would be beneficial, as the Commission has stressed in recent communications¹⁵. Tax co-ordination could contribute not only to eliminating distortions in the single market but also to reversing the long-term trend in taxation structures so as to make them more employment-friendly. In order to counteract tax erosion on the more mobile tax bases, Member States have to some extent been driven to reduce taxes on capital and compensate by overcharging labour. This in turn produces unwanted effects on employment and income distribution.

Objective: Make social protection more employment-friendly by narrowing the gap between total salary costs and net take-home pay for low-skill workers.

Key action: The Commission will deepen the analysis of measures taken to reduce non-wage labour costs as a contribution to the interim report to be presented at the Amsterdam European Council in June 1997 and to the Joint Employment Report to be prepared for the Luxembourg European Council in December 1997; the Commission will, *inter alia*, examine how the trend of increasing levies on labour can be reversed and what practical progress in tax co-ordination between Member States is necessary to allow for a reversal of that trend.

In addition, the permanent High Level tax policy group set up by the Dublin European Council will examine, among other issues, ways of restructuring fiscal systems, including social contributions and taxation on labour.

2.2.4 Implementing flexible systems for managing the transition from work to retirement

The situation of older workers has changed dramatically over the past twenty years. Firms have sought to make employment more flexible, both quantitatively and qualitatively. External flexibility, designed to adjust employment to immediate needs, has been as important as internal flexibility. The result has been, *inter alia*, a steady decline in the employment of older workers.

In order to reduce unemployment and especially to promote opportunities for the young, many European countries have attempted to shorten the working life of the older workforce. Arrangements have been introduced for leaving work well in advance of the retirement age through invalidity schemes, special benefits for older workers, early retirement schemes or by granting pensions early in cases of unemployment. The shortening of working life was the subject of a broad implicit consensus involving employers, workers and the state. Employment rates for over-55s have dropped very significantly in twenty years. The idea of retiring on a fixed pre-established date is disappearing fast.

However, as life expectancy continues to grow and as many Member States are introducing reforms designed to raise retirement ages in order to relieve pressure on public pension schemes (see 2.3.1 below), it is essential to reverse the trend towards early exit from the labour market. The transition to retirement has, paradoxically, become less flexible. Workers' expectations have changed with the massive growth in early retirement opportunities. Where firms have become less willing to invest in training their older workers or in promoting them, the individuals concerned have become less motivated and have often come to see early retirement as the best - or only - option.

Awareness of the challenges associated with early retirement over the coming ten years is poor. The changes now taking place in firms, with younger workers replacing older ones, are unsustainable over time. There are even indications that if current trends continue - i.e. people over 50 or 55 being considered to be unemployable - there could be a shortage in labour force in a number of regions. If serious dislocations are to be avoided and if employment is to be developed in Europe, greater efforts must be made to keep these older workers in the labour market.

¹⁵ In SEC(96)487 of 20.3.96 "Taxation in the EU" and in Communication COM(96)546 of 22.10.96 "Taxation in the EU: report on evolution of tax systems".

This will, in part, involve much more investment in life-long learning for workers than is common today¹⁶. In particular, the Commission is studying possible new fiscal means to promote investment in human resources. It will also require a major shift towards flexible systems for managing the transition from work to retirement and towards systems of part-time employment for older workers. Although the Council adopted a Recommendation as early as 1982 on this topic¹⁷, the arrangements for these more flexible systems are still largely undefined. A key point is to determine to what extent creating incentives for older workers to stay longer in working life can be matched by creating jobs which are adapted to them. Recent initiatives in some Member States should be examined.

Objective: Make social protection more employment-friendly by increasing employment incentives as well as employment opportunities for older workers.

Key action: The Commission will present the potential and problems of a gradual transition to retirement in the Employment in Europe report to be published in September 1997 and will consider appropriate follow-up; the Commission will also invite the social partners to deepen the social dialogue on the impact of ageing.

2.2.5 Social protection to promote inclusion

The modern design of European social protection systems was conceived just after World War II. They were intended to provide workers with a replacement income during periods of work interruption, either temporary (sickness or unemployment) or definitive (permanent work incapacity or retirement). As such, they were quite effective in alleviating poverty. However, social protection is now confronted with a new phenomenon: exclusion.

Exclusion goes beyond poverty. It is the accumulation and the combination of several types of deprivation: lack of education, deteriorating health conditions, homelessness, loss of family support, non-participation in the regular life of society, and lack of job opportunities. Each type of deprivation increases the other types. The result is a vicious circle, leading from long-term

unemployment to the break of family ties, and eventually to marginality and delinquency.

Social protection alone cannot be a remedy for every situation of exclusion. However, social protection has a role to play not only in providing excluded people with an income enabling them to live in keeping with human dignity, but also in helping to reintegrate them into society. Both unemployment compensation schemes and social assistance mechanisms, and particularly the safety nets designed to guarantee a minimum level of resources to all inhabitants, should become essential tools in an active policy to fight exclusion. In particular, it is becoming ever clearer that minimum income schemes, as defined in the Council Recommendation of 1992¹⁸, should be fully integrated into a global policy for fighting exclusion.

At the same time, the role of minimum income schemes has changed. As the number of beneficiaries has grown, the schemes run the risk of becoming a kind of exclusion compensation that confirms social breakdown rapidly, if the schemes are not associated with active integration policies. There is now a growing consensus on the necessity of moving from the traditional social assistance approach.

How can people who are currently excluded be given a role in society? On the one hand, the excluded experience major difficulties in finding a job because they are unable to meet firms' requirements in terms of skills, productivity and flexibility. It is very difficult to require marginalised people to be as productive and flexible on the labour market as skilled and fully integrated workers. In trying to rebuild their lives, excluded people need to be offered integration opportunities with a guaranteed minimum level of stability. This minimum stability is not easy to find in the private, profit-making sector of the economy.

On the other hand, there are needs which are not currently met in the sector of non-market services, run by central Government, local authorities and the NGOs. Several Member States have embarked on a new approach, aiming at the activation of social assistance expenditure and trying to achieve long-lasting integration of excluded people through meeting social needs which are currently financially out-of-reach. The same experiments are made both by the countries which are most advanced in terms of active labour market policies and by the countries

¹⁶ See White Paper on Education and Training: "Teaching and Learning: Towards a Learning Society", COM (95) 590.

¹⁷ Council Recommendation 82/857/EEC of 10 December 1982 on the principles of a Community policy concerning the age of retirement, OJ L 357 of 18 December 1982.

¹⁸ Council Recommendation 92/441/EEC of 24 June 1992 on common criteria concerning sufficient resources and social assistance in social protection systems, OJ L 245 of 26 August 1992.

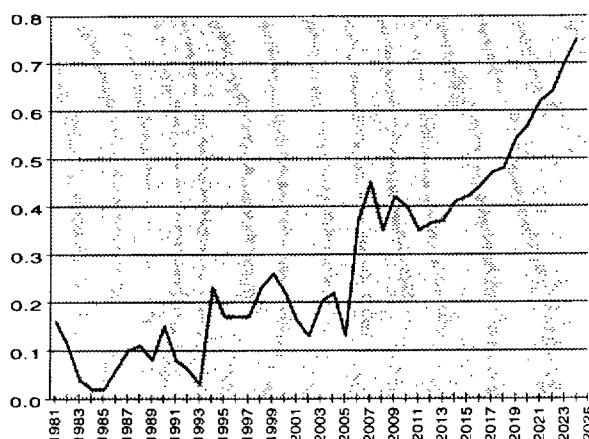
which are making efforts to develop the integration part of their minimum income schemes. They need to turn a passive and precarious solidarity with excluded people, into a contract that offers them real opportunities of both social and economic integration, in return for a commitment to make an effort themselves. However, this boost for non-market activities must be carefully monitored and some links with market activities must be developed in order to avoid a further segmentation of the labour market and some people being locked into subsidised jobs.

Objective: Make social protection more employment-friendly by activating integration policies associated with social minima benefits.

Key action: In the first half of 1997, the Commission will present a Communication on the promotion of social inclusion and, in the second half of 1997, a report assessing the mechanisms of guaranteed minimum income schemes in the social protection systems of the Member States. These documents will examine the details of integration contracts (duration, conditions of transition towards regular jobs, etc.) and how such a policy can be made sustainable for public budgets.

A recent study has examined national projections of pension expenditure for the EU-15 for the period 1995-2030²⁰. Projections are based on unchanged policy scenarios but take into account the major reforms that have been introduced in Member States since the mid-eighties. Over the period 1995-2030, the increase in the EU average ratio of pension expenditure to GDP is likely to reach 3 or 4 percentage points (from 12% to 15 or 16%). By the year 2030, in several countries (Belgium, Finland, France, Germany, Italy and the Netherlands), the ratio of pension expenditure to GDP might be in the range of 15 to 20%. Expenditure would be lower in Denmark, Spain, Sweden (in the 10 to 15% range), and in Ireland and the United Kingdom (below 10%).

Amount of annual gain in labour productivity needed to compensate the effect of ageing European Union (15)



2.3 Adapting social protection to the demographic ageing of European societies

2.3.1 Making public pension schemes sustainable

The demographic structure of European countries is changing considerably¹⁹. The old-age dependency ratio (i.e. the ratio of older people to working age population) is increasing in most countries and reaching historically unprecedented levels.

Although the long-term effects of the ageing process on public budgets are rather uncertain and depend on the way the economy will adapt to the process, a significant pressure towards higher public expenditure is very likely to occur in the coming decades. Public pension schemes will bear much of the pressure since their expenditure is highly dependent on the age structure of the population.

The ageing of the population in Europe has triggered a debate on the viability of our current public pension systems and on alternative ways of making pension systems stable. In principle, there are two ways of funding a pension system. One is to agree on a mechanism which sets out how workers will get transfers when they are retired, in exchange for the contributions they give today to pensioners. This is the pay-as-you-go system (PAYG). Pension benefits are calculated on the basis of a formula fixed in advance and are usually dependent on years of service and average or final salary. They are financed through contributions from employees and employers and budget transfers. The operation of such systems depends on the contributor's willingness to pay. This in turn is conditioned by their expectations that adequate transfers will continue in the future.

19 The report on "The demographic situation in the European Union", 1996, addressed in detail the medium and long-term demographic perspectives in EU Member States". The charts annexed to this communication show the population growth between 1995 and 2015 for three age groups in the different EU Member States.

20 D. Franco and T. Munzi, "Public Pension Expenditure Prospects in the European Union: A Survey of National Projections", European Economy, Reports and Studies N° 3, 1996.

The other funding method is to base the transfer of income, not on the promise that it will continue in the future, but on property or financial assets (funded schemes). Such schemes are, as a rule, funded through regular contributions and provide benefits dependent only on the return on assets invested. Consequently, pension income is subject to inflation and investment risk.

The debate and research on alternative ways to fund pension schemes has led to some important conclusions. First of all, there is no escaping the fact that current GDP is shared every year between those who receive income directly from their participation in economic life and those who do not. That goes for the PAYG as well as the funded schemes.

Secondly, a radical transformation of the public schemes from PAYG to funded schemes is not realistic because of the huge transition costs. In the case of a sudden shift, all members of the pension schemes and their liabilities would be transferred to the funded schemes at once. In this case, all liabilities of the current schemes would become explicit, i.e. the stock of government debt would increase at once. In terms of cash flow, expenditure would continue, but without any incoming contributions. If the outgoing pensions are financed in full by an increase in government borrowing, the burden of the transition would be distributed over all future generations. If it is only partly financed through increased government borrowing and partly through increased taxation, the burden of fiscal consolidation would fall on the current generation which would pay twice, while future generations would benefit. A gradual transition, i.e. only new entrants in the labour market participating in the funded schemes, would create constant pressure on primary balances throughout the transition period. Both would be problematic in the current fiscal environment.

Given that a wholesale switch to funded schemes appears to be an unrealistic solution, most Member States are focusing on ensuring sustainability of the public PAYG schemes. This will require the implementation of significant reforms. The most important one is to find mechanisms to allow people to work instead of taking early retirement, that is to say to increase the actual pension age, now below 60 and falling, while maintaining the formal pension age, generally 65. This will both increase contributions and reduce payments. If this is not possible, the options available include, in theory, raising contribution rates, increasing budgetary transfers, reducing benefits or a combination of the above.

Most European countries have changed the indexation of pensions from income or wage

increases into indexation on prices. More fundamental reforms carried out in recent years by some Member States (Belgium, Finland, France, Germany, Italy, Sweden) show certain common features. The timing of retirement is no longer determined simply by a statutory retirement age but, equally important, by the number of contribution years necessary to have a full pension. A few Member States have adopted the principle of flexible retirement within a given time span. In terms of equity, these are positive developments. The charge has occasionally been levelled at European systems that they are in effect anti-redistributive (i.e. benefiting the rich at the expense of the poor) in the sense that life expectancy correlates positively with income. The scale of this anti-redistribution is diminished by moving to flexible retirement arrangements, in so far as the age of joining the labour market is itself positively correlated with income.

Another common trend is the closer link being forged between pension levels and total contributions made during working life. This concentration on the contributory side of pension systems makes sense at a time when boosting the incentive to work is a priority. It does, however, call for the solidarity element in each pension system to be made explicit: by how much should the pension be reduced to take account of career breaks - caused by unemployment, illness, child-care or elder-care? The danger is that women, whose working lives are less linear than men's, will be penalised through this development. In the longer term, this trend could also work against the kinds of changes taking place in the working life-cycle, such as time taken off work at intervals to update skills.

Objective: Foster the adaptation of public pension schemes to the ageing of European populations.

Key action: Develop comparable projections of pension expenditure using common forecasting methodologies and harmonised economic and demographic assumptions; assess the elements of reform which seem to be most adapted to ensuring the sustainability of public pension schemes while preserving their core aspects of solidarity and present the conclusions in the Social Protection in Europe report to be published at the end of 1997.

2.3.2 Providing a secure environment for supplementary pension schemes

In addition to ensuring the sustainability of the public pension schemes, it will be increasingly important to ensure that current employees and future pensioners are in a position to maintain post-retirement income at a level that will enable them to avoid a drop in their standard of living. One way of achieving this is to encourage the development of supplementary pension schemes operating on a fully-funded basis. Pension funds can be expected to stand side by side with the public PAYG schemes in those states where the development of such schemes takes hold. Whether such schemes do take hold will be a matter to be decided by the Member States.

As the importance of supplementary pensions increases, it becomes more important for governments to provide a secure environment for the efficient operation of supplementary funded schemes. All Member States have rules of prudential management. At Community level, Directives 80/987/EEC and 77/187/EEC²¹ ensure the safety of assets, notably in the event of an employer's insolvency or the transfer of an undertaking. If workers can individually choose a financial institution for their retirement provision they should have access to understandable information helping them to make the right choices and avoid pension levels which remain below their expectations.

In the context of the single market, there is an opportunity for making the development of funded occupational schemes more effective, for the benefit of scheme members and the economy as a whole. This can be achieved through the Treaty rights of free movement of capital and free provision of services. The freedom of capital movements guaranteed by Article 73b of the Treaty enables pension funds in all Member States to diversify their assets, both domestically and internationally. This should enhance returns, reduce risks arising from domestic economic cycles and reduce the negative impact on asset prices during periods of disinvestment, when elderly generations realise their wealth. However, the freedom of capital movements can be seriously restricted by currency matching rules imposed by the Member States for prudential reasons.

The regulatory framework must also implement the principle of equal treatment for men and women. The 1996 "Post-Barber" Directive²², following several judgements of the European Court of Justice, sets out the principles for this implementation. The practical application of these principles in the management of pension funds should not work to the disadvantage of women, who should not be penalised for their greater than average longevity. This could happen through, for example, a reduction in take-home pay, because of a requirement to pay extra contributions, or from a reluctance on the part of employers to recruit women because they represent higher employment costs than men performing the same work, due to higher contributions.

The difficulty in achieving equal treatment demonstrates the need to regulate the mechanisms of supplementary pension systems. Social protection - in contrast to private insurance - seeks through a large-scale pooling system to separate the level of individual risk for each insured person from the contributions paid by individuals or their employing organisations. This is designed to avoid bad risks being penalised, either through lower net salaries or through higher employment costs. This pooling of risks is more difficult to achieve in the limited context of supplementary defined benefit schemes and is absent from defined contribution schemes. Even though funded supplementary schemes are not grounded in solidarity, it is important to ensure that there is fair treatment of all schemes members, including those such as part-time workers or those who take career breaks, especially given the expected increase in importance of such schemes.

Innovative approaches will need to be found if the growing importance of supplementary schemes is not to lead to a breakdown in the principle of solidarity. In particular, it would be damaging to those in non-standard or precarious occupations (part-timers, career-breakers) to be left without a fair coverage by occupational schemes.

21 Directive 77/187/EEC - OJ L061 of 5 March 1977 - on the approximation of the laws of the Member States relating to the safeguarding of employee's rights in the event of transfer of undertakings, businesses and Directive 80/987/EEC - OJ L283 of 20 October 1980 - on the approximation of the laws of the Member States relating to the protection of employees in the event of the insolvency of their employer.

22 Directive 96/97/EEC of 20 December 1996 - OJ L046 of 17 February 1997 - modifying Directive 86/378/EEC concerning equality between men and women in occupational social security schemes.

Objective: Provide a secure environment for supplementary pension schemes.

Key action: In the first half of 1997, the Commission will issue a Green Paper on supplementary pensions with a view to identifying, with all parties concerned, including the social partners, the main elements of a framework at European level to provide a secure environment for the efficient operation of supplementary funded schemes.

2.3.3 Meeting new care needs for older people

As our societies change, so do our needs in terms of social protection. Life expectancy has increased considerably since the immediate post-war years, and old age can in general no longer be considered as a difficult time in economic terms. However, new needs are emerging in relation to living conditions in the final phase of people's lives and the ageing of Europe will have a particularly strong impact on care needs.

Advances in the treatment of acute illnesses as well as the general increase in life expectancy means that a growing number of people spend their last years in a state of dependency on others for the day-to-day basics of life. Until now, care in these cases was often provided informally by family members. This form of family solidarity is becoming less feasible, however, as more women work outside the home and as greater geographic distances separate parents from their adult children. All European countries subscribe to the objective of enabling older people to stay in their own homes if at all possible rather than enter a care institution. The older people concerned clearly share this wish.

Amongst the enabling conditions for dependent older people to live at home is the availability of medical and paramedical care as well as home help for day-to-day needs. The cost of these services, taken over a number of years, can be very high. In several countries, there is a strong fear that voluntary insurance for dependence along these lines could give rise to the phenomenon of adverse selection and moral hazard. These make cost forecasting - and thus premium fixing - very difficult. The end result could well be a risky and therefore unattractive product for private insu-

rance companies. In the case of voluntary insurance, there is also the fear that a large part of the population will underestimate the risk which they face and will choose not to take out the necessary insurance in time.

Thus we are witnessing the emergence of a new branch of social protection. The economic as well as social interest in compulsory cover of the population against the risk of dependence appears well founded. However, it is not easy to reconcile the need to meet these new care needs with the imperative of containing the relevant care costs. The main questions concern the type of cover given by a system of compulsory insurance: services or money - the latter giving a greater choice to beneficiaries; the way to evaluate care needs and to manage delivery of benefits in accordance with needs, and the advantages and disadvantages of targeting benefits and selecting beneficiaries based on their income.

In any case, a growing need for social services will emerge, the satisfaction of which has a great employment potential, and requires careful policy-design. Special attention should be paid to equal opportunities with respect to the new jobs created in the caring sector to prevent the emergence of a gender imbalance. Finally, the delivery of services must meet high quality standards.

Objective: Revisit social protection systems to meet the care needs of dependent older people.

Key action: Analyse in the 1997 Social Protection in Europe report the experience of Member States which have already implemented care-related provisions with a view to identifying the most efficient patterns of a long-term care insurance scheme.

2.3.4 Improving health services

Each Member State's health system is different as it reflects a unique pattern of historical and cultural developments. Nevertheless, the systems in the European Union fall into two basic groups: either mixed systems which make use of services from both private and public organisations financed mainly from compulsory health insurance contributions; or national health services in which provision and financing is mainly located within the public sector.

Total expenditure on health in the Member States varies from just over 5 to nearly 10 per cent of GDP. Expenditure in absolute terms has been rising for many years and all Member States are experiencing mounting pressure on their health services. For instance, per capita expenditure for health care for the very old is five times as high as for a person of working age. As the age group 75 and over will increase by nearly 50% during the next 20 years, it will have a significant effect on total health care expenditure. This development arises not only from demographic change, but is also a result of rising expectations of what health systems can and should provide.

The pressures on health systems have led to a number of reform initiatives in the Member States with the aim of improving both the overall effectiveness of health provision in terms of health gain and of the services' efficiency. The 1995 report on the State of Health in the European Union²³ outlined some of the reforms being undertaken and also confirmed that Member States are giving more prominence to disease prevention and health promotion activities in the belief that modest investments in these areas will have a significant impact on the powerful factors affecting the main causes of mortality and morbidity. Following earlier unsuccessful attempts to contain the costs of public health systems, e.g. by increasing co-payment, a number of Member States are now trying to introduce market mechanisms into their health care systems in recent years. One particularly notable reform has been the separation between the functions of purchasing services and their delivery. Hospitals and other service providers enter into contracts with local health authorities for the provision of particular services. In this way, these authorities are forced to define their requirements more clearly and seek the most cost-efficient ways of meeting them. Competition between service providers is thus encouraged.

There are clearly risks that in the search for cost savings both providers and authorities will be tempted to go for the cheaper rather than the optimal solution. Moreover, there have also been examples of contracts which are imprecisely drawn up in terms of what is to be delivered and to what standard. However, it is still much too early to make definitive judgements about the consequences of these and other measures.

In the quest to improve the efficiency of health systems, putting health care insurers - private or public - in competition with each other, while establishing the proper regulatory framework and guarantees, is attempted in some Member States. It is essential to exclude elements, such as risk selection, which may deprive individuals

from the necessary cover. On the other hand, subject to proper conditions to avoid distorting effects, each insurer should be able to contract with those service providers which will provide them with the best services at affordable prices. The combination of these factors may well lead to a reduction in costs, although the greater gains are bound to be found in health care costs rather than in the management of the insurance activity itself.

In these conditions, it is crucial that the freedom to provide health services and place relevant products on the internal market is underpinned by such a framework so as to benefit the health systems and result in continuity and affordability of health care across the Community. Such a framework can be constructed on the principles of facilitating the timely sharing of validated information on the comparative merits of interventions, the efficiency and cost-effectiveness of new technologies, encouraging the transfer of know-how in service organisation, promoting the optimal utilisation of existing resources, in particular in border areas, and minimising the number and extent of additional administrative arrangements applicable to users of services from other Member States.

Objective: Improve the efficiency, cost effectiveness and quality of health systems so that they can meet the growing demands arising from the ageing of the population and other factors.

Key action:

- carry out an assessment of the potential impact of prevention on the reduction of health care costs;
- clarify to what extent and under what conditions, introducing market forces within health care systems can help save costs while fostering a better quality of services and ensuring access for all to health care;
- the Commission will bring together work carried out in the Member States on the efficiency and cost-effectiveness of health care systems, and assess which initiatives can be taken at Community level to assist Member States in reducing costs while maximising health gains.

23 COM (95) 357 of 19 July 1995.

2.4 Adapting social protection to the change in the gender balance: towards an individualisation of rights

Female participation in the labour market will continue to increase during the years to come. In order to maximise the potential contribution of women, it is essential to adapt social protection to the new gender balance. This implies:

- i) finding new arrangements for reconciling working and family life;
- ii) implementing progressively an individualisation of rights.

The changing pattern of household composition and family types requires new responses. Innovative and viable schemes need to be developed to reconcile working life with the needs of families, households and individuals, while avoiding putting the burden for all care on families. In line with the commitments of the Fourth Action Programme for Equal Opportunities for Women and Men (1996 - 2000)²⁴, the Commission is exploring a range of practical initiatives and policy options, including consideration of measures aiming at setting higher standards for the care of children and other dependants. At the initiative of the Commission, the social partners reached an agreement on parental leave giving men and women an individual right to parental leave with the guarantee of being able to return to the former workplace after the leave period. The agreement was adopted as a Council Directive on 3 June 1996²⁵.

In virtually all Member States, the social protection system contains elements which connect the social protection of an individual to his or her specific family situation, single, married, cohabiting, etc. In the past, such derived rights have been successful in protecting many people from poverty. They take account of family links, the value of work at home and care work and give those who have not participated on a continuing basis in paid work in order to serve their families the security of an income after the death of the breadwinner. In that respect, splitting pension credits between partners in case of divorce could be seen as a recognition of the implicit contribution of the non-active or low-paid partner.

However, derived rights pose certain problems. They create dependency on the person who has a direct entitlement to social security benefits.

Direct social security rights being, in most cases, acquired through paid employment, the lower participation of women is reflected in a lack of direct rights. Women are therefore more vulnerable when a relationship breaks down, e.g. in cases of divorce. Furthermore, derived rights are, in most countries, given to spouses and children only. They do not always take account of other forms of cohabitation which are increasing.

Secondly, derived rights can create disincentives for women to enter the labour market and can lead to incentives to take up jobs in the informal, unprotected economy. In some countries, marginal employment does not provide access to social security at all. This is only tolerated because the marginally employed generally benefit from derived rights and their work is not regarded as an independent way of making a living, but rather as a supplement to the family budget, leaving the person in question to depend on the social security of their partners.

Finally, survivors' pensions enable people to benefit from a pension on the strength of the contributions of his/her deceased spouse without the former having had to make any additional contribution. This can lead to the situation whereby a spouse who has never worked outside the home can receive a higher pension, calculated on a complete career and high income of the deceased spouse, than a single person having worked all his/her life with a lower income. As a result, derived rights tend to re-distribute social security benefits from the average income earner to the dependants and survivors of the high income earners.

The individualisation of rights would aim to halt the practice of taking account of personal links when ensuring social protection of an individual. It would contribute to bringing social protection in line with legislation governing employment contracts, which considers workers as individuals. More generally, individualisation is in line with the general trend towards a greater autonomy of the individual. In that sense, it goes beyond gender issues and also concerns the relations between parent(s) and children in the light of new family patterns and structures.

Admittedly, the individualisation of rights could lead to hardship. For instance, derived rights can give the unemployed indirect entitlement to benefits for dependent children. Individualisation could also lead to specifying the age

²⁴ COM(95)381 of 19 July 1995, JO C306 of 17 November 1995.

²⁵ Council Directive 96/34/EEC of 3 June 1996 on the Framework Agreement on parental leave concluded by UNICE, CEEP and the ETUC OJ L145/4 of 19 June 1996.

requirements for entitlement to benefits. Nevertheless, a strategy must be devised to encourage all potential workers to participate in the labour market in their own right without putting undue strain on family finances.

The individualisation of rights would have different effects on the individual as well as on public budgets depending on the branch of social protection considered. Individualising entitlements to health care and unemployment benefits seems to be relatively straightforward due to the small budgetary effect it probably would have. The most important and the most difficult branch to individualise would be retirement pensions, which is the area where the bulk of derived rights is granted. Not only would individualising mean abolishing supplements for dependants but it would also mean replacing the survivor's pension with another type of replacement income. For widow(er)s under the retirement age a special transitional pension could be granted until the retirement age or until a job is found.

Given the current position of women on the labour market, it is most probable that taken as a group, they would lose considerably if survivor's pensions were abolished, and many could even fall below the poverty line. The idea of a basic old-age pension supplemented by an occupational pension might be able to accommodate this very complex problem, the first element assuring that all above the retirement age would receive a sufficient amount to enable them to provide for themselves. But the current trend in Member States' pension reforms is going in the opposite direction, i.e. establishing a closer link between contributions paid through employment and the amount of pensions (see 2.3.1 above), thus making the solution of this problem more difficult. An in-depth reflection on the impact of career breaks on pension rights is necessary in order to find ways of overcoming this apparent conflict of objectives. In that respect, Member States should learn from the diversity of approaches that exist within the Union.

Objective: Adapt social protection to the new gender balance in working life and to changes in family structures.

Key action:

- the Commission will present initiatives aimed at setting higher standards for the care of children and other dependants;
- the 1997 Annual Report on Equal Opportunities will assess the attempts made by the Member States to make progress towards individualisation without jeopardising the economic situation of women.

2.5 Improving social protection for people moving within the Union

Regulation 1408/71, based on Articles 51 and 235 of the EC Treaty, co-ordinates social security arrangements for people moving within the Union. It is a prerequisite for the free movement of workers. This regulation provides a high standard of protection for people moving between Member States.

However, there are still a number of gaps in the protection offered by Regulation 1408/71²⁶. Moreover, the co-ordination system, as it currently stands, is in danger of becoming outdated and losing touch with a number of developments. Member States have recently introduced new types of benefit, for example those for an increasingly ageing population requiring long term care, which cannot be easily accommodated within the legal concepts contained in Regulation 1408/71, based on the classical branches of social security. The introduction of new forms of social protection in the Member States should not be hindered by uncertainty about the possible impact of the co-ordination system on the new schemes.

The original dimension of European integration, i.e. a common market allowing and fostering free movement of workers, has been enriched by a new concept, namely that of European citizenship. The personal scope of Regulation 1408/71 should be adapted accordingly.

The co-ordination of the various national social security schemes is inevitably complex. However, unnecessary complexity should be avoided and rules should be simplified wherever possible. The aim should be to make the rules more easily

²⁶ A number of these gaps have been discussed in the Commission's Green Paper "Education, Training, Research: The Obstacles to Transnational Mobility" COM (96) 462.

understandable for citizens moving within the Union and to overcome practical problems and red tape in the day-to-day application of the Regulation, which can obscure the advantages which it aims to provide. The Commission will develop a strategy to simplify and reform the co-ordination system so that it meets current and future requirements. The national authorities and institutions, the European Parliament and the social partners will be closely involved in the development of such a strategy.

The opinion has been expressed on many sides during the debate that it is no longer justifiable that a worker who is insured and legally residing in a Member State, and therefore covered by national social protection arrangements, should be completely excluded from the protection offered by the co-ordination system simply because he or she is not an EU national. In the second half of 1997, the Commission intends to present a proposal to the Council aimed at extending, wholly or partially, the co-ordination provisions to employed and self-employed persons insured in a Member State who are not EU nationals.

The debate also demonstrated a need for in-depth discussion on the current provisions on cross-border access to health care, notably with a view to permitting greater and more efficient use of existing facilities, especially in border regions. However, the consequences for the financial equilibrium of health insurance in the Member States should be taken into consideration and the financial provisions in the co-ordinating Regulations in relation to health care should also be re-examined. Subject to the judgements of the Court in the Decker and Kohll cases²⁷, the Commission will present a proposal to amend Regulation 1408/71 in order to facilitate cross-border access to health care services.

Furthermore, the fact that there is no Community co-ordination of taxation, while social security is subject to co-ordination, sometimes creates anomalous situations; for example in the case of certain frontier workers who may be obliged to pay twice for social security - on the basis of high taxation in the state of residence, and via high insurance contributions in the state of work. The Commission intends to investigate these problems during 1997 and identify ways in which action at Community level could overcome them.

There is a broad consensus that the absence of any co-ordination system at European level for supplementary pension schemes constitutes a real problem for persons moving within the Union. This is particularly the case in those Member States where occupational schemes play an important role in social protection. The Commission's Communication of July 1991²⁸ identified the particular obstacles in this field. Given the specific nature of many of the schemes in question and their extreme diversity at national level as regards their origin, their occupational and material scope, as well as their legal and technical forms, the current co-ordination system created for statutory schemes does not seem to be the appropriate instrument to address the problems. A more flexible approach is required. The report of the High Level Panel on Free Movement of People chaired by Mme Simone Veil²⁹ suggested to the Commission a way forward in this area. The Commission will consider all the obstacles to free movement arising in this area in the framework of a Green Paper on supplementary pensions which will be published shortly. It intends, however, as a first step towards dealing with these obstacles, to present a proposal for a directive which should in principle cover the aspects highlighted by the High Level Panel's report.

Objective: Adapt the co-ordination system to new forms of social protection and new needs in the field; avoid unnecessary complexity and remove barriers to cross-border mobility.

Key action: - The Commission will develop a strategy both to reform and simplify and to update the co-ordination system, closely involving national authorities, the European Parliament and the social partners.
- The Commission will publish a Green Paper on supplementary pensions in which all the obstacles to free movement arising in this area will be considered. As a first step towards dealing with these obstacles, the Commission intends to present a proposal for a Directive which should in principle cover the aspects highlighted by the High Level Panel's report.

27 The Court of Justice is currently examining the extent to which the current provisions of Regulation 1408/71, which permit access to cross-border health care, at the expense of the competent State, only under strict conditions, are compatible with Article 30 EC Treaty (free movement of goods such as pharmaceuticals) and Article 59 EC Treaty (freedom to provide services such as health care services): Cases Decker (C-120/95) and Kohll (C-158/96).

28 Communication of the Commission to the Council, "Supplementary social security schemes: the place of supplementary pension schemes in the social protection of workers and their effect on free movement" SEC(91)1332.

29 Report on supplementary pensions adopted at the meeting of 28/29 November 1996 of the High-Level-Panel.

3. SUPPORTING THE ADAPTATION PROCESS THROUGH ACTION AT EUROPEAN LEVEL

This Communication is based on the principle of subsidiarity. Each Member State is responsible for the organisation and financing of its own social protection system. The Union remains responsible for the co-ordination of social security schemes as regards the protection of people who make use of their right to move within the Union. Moreover, the exchange of experience between the Member States represents important added value at EU level.

Modernising and improving social protection in the Union cannot be achieved without the active participation of all involved. In part II of this Communication, the Commission has announced a number of key actions aimed at setting out both orientations for achieving that goal and more concrete steps for further reflection.

The Commission invites the Council, the European Parliament, the Economic and Social Committee, the Employment and Labour Market Committee and the Economic Policy Committee to give their opinions on the ideas for the modernisation of social protection systems presented in this Communication.

The Commission invites the social partners, at all appropriate levels, to contribute to the debate, in particular with regard to the three following points:

- impact of the ageing of the population on the transition to retirement;
- details of a regulatory framework at European level to provide a secure environment for the efficient operation of supplementary schemes;
- implication of the development of new patterns of work, and especially the impact of career breaks on social security rights.

Social protection issues will have to be integrated into the development of European employment policy. Today, employment is the first priority for the European Union and the Member States and their greatest challenge. This commitment creates both a need and a potential for fur-

ther action at Community level. The Commission will make a contribution to this process in the Single Report which will be presented to the European Council in Luxembourg in December 1997. This contribution will analyse the reforms already implemented by the Member States to make social protection more employment-friendly and will propose further lines of action. The Group of Directors General for Social Security will be invited to contribute to the preparation of this report.

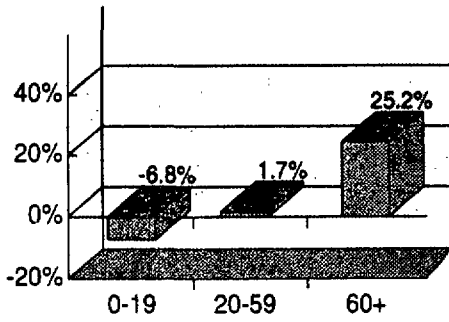
This process of common reflection must also involve a wider range of participants, including the representatives of civil society. The whole issue will be at the top of the agenda of the 1998 *European Social Policy Forum*. The forum will involve Member States, the social partners and NGOs, as well as European institutions. It will discuss the direction of the reforms of social protection systems for the next decade. More specifically, ways of adapting social protection systems to the new needs described above will be a key issue for that discussion.

Finally, the *Social Protection in Europe* report, to be published at the end of 1997, will bring together more evidence and analysis on recent developments in Member States, as a contribution to the process of joint reflection.

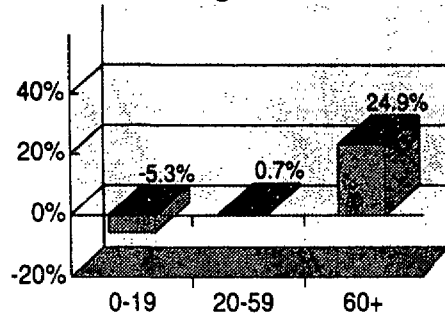
Appendix

Population growth between 1995 and 2015 for three age groups
Central scenario

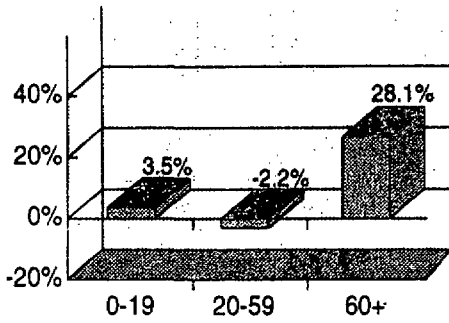
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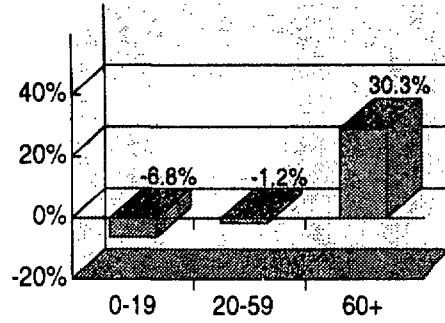
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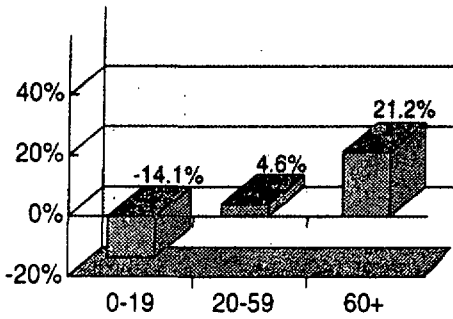
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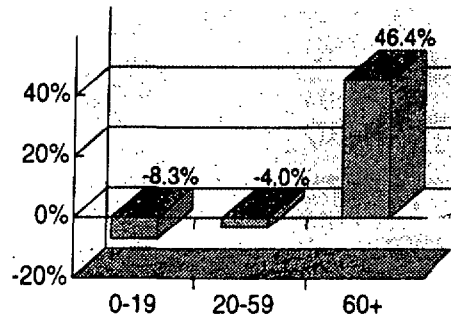
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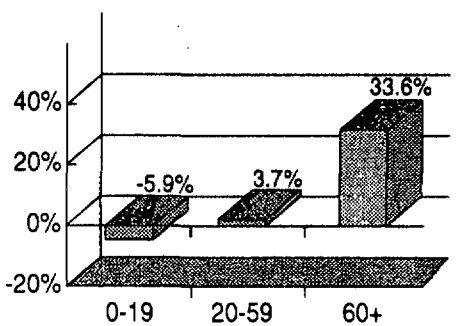
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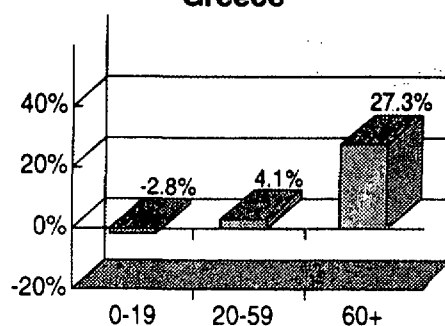
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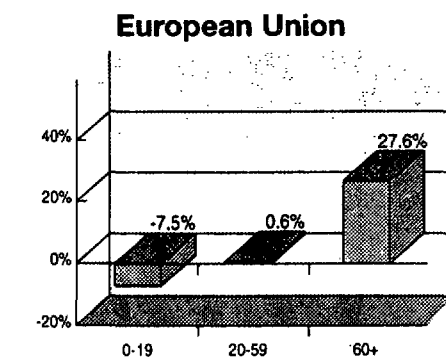
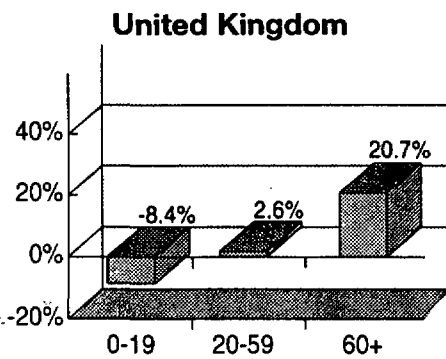
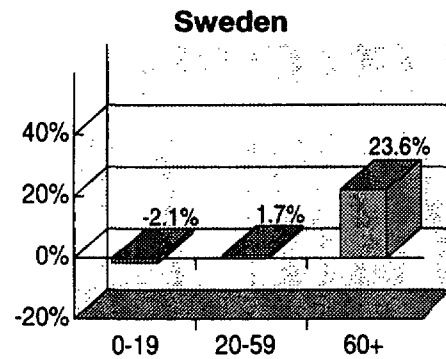
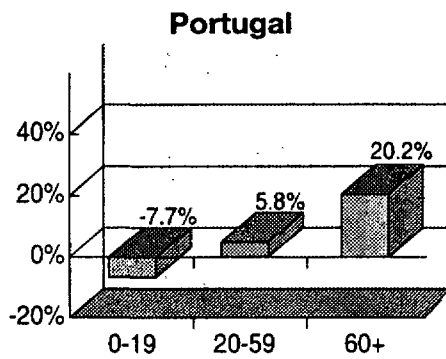
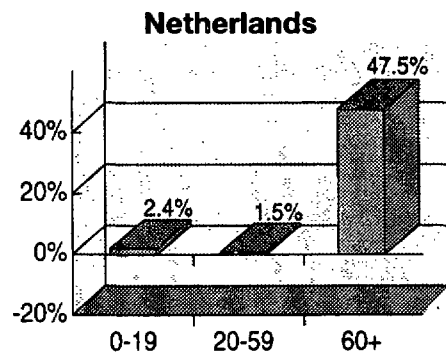
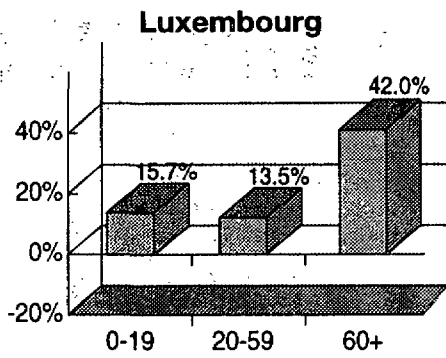
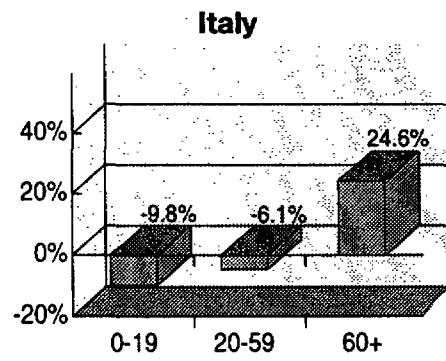
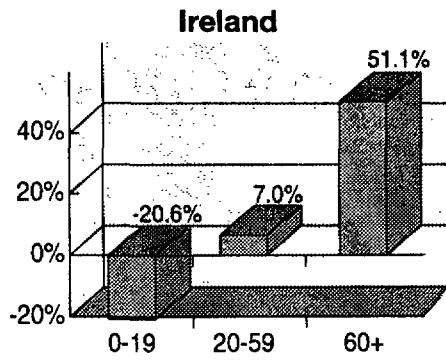


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