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THE FUTURE OF SOCIAL PROTECTION:
A FRAMEWORK FOR A EUROPEAN DEBATE

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THE FUTURE OF SOCIAL PROTECTION :

A FRAMEWORK FOR A EUROPEAN DEBATE

1. A NEW INITIATIVE: WHY?

1.1 A common feature of European societies

Social protection represents a fundamental component and a distinguishing feature of the European model of society. It is a major achievement of post-war Europe, which has enabled societies to cope with a period of tremendous economic and social adaptation. There continues to be a large degree of consensus that it is the responsibility of governments to ensure that nobody is left deprived when poor, sick or disabled. Social cohesion is an objective of all European countries as much now as in 1945.

Social protection¹ can be defined as all the collective transfer systems designed to protect people against social risks. Whilst there is significant diversity among national systems, all 15 Member States provide specific income maintenance benefits to cover the classic risks of old age and retirement, the death of a provider, disability, sickness, maternity, dependent children and unemployment. And in some countries, other contingencies are also covered, such as the cost of caring for frail elderly, disabled or sick relatives, and sole parenthood.

Social protection is therefore an essential component of solidarity between the peoples of the Member States of the European Union, resulting both from its aim to provide universal coverage and the absence of a proportional link between contributions levied to finance the system and the individual vulnerability of the persons covered.

Throughout the European Union significant reforms of systems of social protection are now under consideration, and in a number of cases being introduced, in response to the need to adapt to rapidly changing social and economic conditions, to contain costs, and to replace the old rigidities with more flexibility, while at the same time maintaining this objective of solidarity.

¹ In this document the word "social protection" is used because it is more comprehensive than other terms such as social security, and because there is a common definition, through the Eurostat ESSPROS statistics.

In this context, it is clear that each Member State remains responsible for the organisation and financing of its own particular social protection system. However, given the common challenges facing Member States in this area, there is considerable value in launching a debate on these issues at European level.

1.2 How far have we got?

Maintaining a high level of employment and social protection is one of the Community's fundamental objectives and explicitly included in the tasks listed in Article 2 of the Treaty on European Union. At Community level, the legislative process has concentrated up to now on applying the fundamental principles of the Treaty to social protection. As a corollary of the freedom of movement, social security for migrant workers is the subject of a coordinating mechanism of legal schemes, based on Article 51 and founded on regulations 1408/71 and 574/72 and on their successive amendments². As an application of a fundamental legal principle of equality for men and women and of Community policy relating to equal opportunities, directives were adopted in 1978 dealing with equality of treatment within legal schemes and in 1986 within occupational schemes³.

For historical and cultural reasons, social protection is not conceived, organised and funded in the same way in all the Member States. One important difference is the role of the State, of social partners and of private enterprises in the decision-making process and in the management of the system. Across Europe we can find statutory schemes run by the government or by non-profit making bodies, managed by social partners for example. For supplementary schemes, the variation is even wider⁴. Nonetheless, however different the social protection systems are, they are all facing very similar challenges.

² The aim of these regulations is to allow migrant workers to aggregate insurance periods accumulated in the Member States where they exercise their activity and to transfer any rights acquired during such periods.

³ Directive 79/7/EEC (OJ N° L 6 of 10 January 1979) and Directive 86/378/EEC (OJ N° L 225 of 12 August 1986); see also the proposal for a Council Directive amending Directive 86/378/EEC adopted by the Commission on 16 May 1995 (COM(95) 186-final).

⁴ See: "Supplementary Pensions in the European Union", Social Europe, supplement 3/94, European Commission, Directorate-General for Employment, industrial relations and social affairs.

In the light of this, the Commission proposed in 1991⁵ a convergence strategy for social protection which was approved by the European Parliament⁶ and the Economic and Social Committee⁷.

Based on this, the Council adopted two Recommendations in 1992, one on the convergence of social protection objectives and policies⁸ and the other on common criteria concerning sufficient resources and social assistance in social protection systems⁹. In these Recommendations, the Member States have agreed jointly on the need to maintain, adapt, and in some cases, develop their social protection systems and have set themselves common objectives.

This strategy for the convergence of policies while abiding by the diversity of systems has helped to improve the exchange of information between the Member States. The Commission is now issuing a Report on Social Protection in Europe¹⁰ every two years, this setting out detailed information on and analyses of the social protection systems in the Member States of the Union and the policies implemented by each country.

1.3 The reasons for a European Debate

The developments in Community policy since 1992, notably the Community-wide framework for employment presented by the Commission in 1993¹¹ and the White Paper on Growth, Competitiveness and Employment presented to the European Council in Brussels in December 1993, call for more extensive joint reflection on this matter. In particular, some of the means for improving the employment situation in the Community, defined at the Brussels, Corfu, Essen and Cannes European Councils refer to social protection and its funding, whether by reducing indirect labour costs or through the combined effects of tax schemes and aid schemes on readiness to offer and to take up jobs.

In addition, the Ministers responsible for social security, meeting at an Informal Council in Paris on 2 February 1995 for the purpose of discussing the financing of social protection, recalled their commitment to the European social model and wanted to reinforce the effectiveness of coordination.

⁵ Proposal for a Council Recommendation on the convergence of social protection objectives and policies, (COM(91) final), OJ C 194 of 25 July 1991.

⁶ OJ C 67 of 16 March 1992.

⁷ OJ C 40 of 17 February 1992.

⁸ Recommendation 92/442/EEC of 27 July 1992, OJ L 245 of 26 August 1992.

⁹ Recommendation 92/441/EEC of 24 June 1992, OJ L 245 of 26 August 1992.

¹⁰ COM(93) 531 and COM (95) 457

¹¹ COM(93) 238.

Accordingly, the Commission included in its medium-term social action programme 1995-97¹² a proposal for a framework for debate on the future of social protection to promote common reflection between the Member States on these issues, that is a programme for reflection in the medium term, based on contributions from all the parties involved.

The purpose of this communication is to spell out the aims of this framework and the ways it can be developed, by both the Member States and the Commission.

2. THE NATURE AND SCOPE OF THE PROBLEMS

2.1 Employment and social protection

In all the Member States, social protection systems were set up in a context both of relatively low rates of activity, especially for women, and low unemployment. They were not designed to cope with the current imbalance between demand for and supply of jobs. The burden of the transfers to persons not in gainful employment, whether retired, sick, incapable of working or unemployed, has grown for those whose income comes from economic activity. The resulting indirect labour costs are seen as prejudicial to the development of employment, competitiveness and economic growth. Moreover, the combination of means-tested benefits and the taxes levied on income from employment can be such that the unemployed have little or no incentive to seek employment.

Social protection is also crucial to the very working of our societies. There has been a large degree of success in combating poverty, especially among older people, disabled people and large families. In times of recession the income transfers produce *countercyclical effects* at macroeconomic level. Social protection has *facilitated the access to education* for lower income families and thus has contributed to improve the quality of the labour force. It has helped to cushion the social effects of industrial restructuring, and thereby *facilitated economic progress*. In the current period it is essential to *alleviate the social effects of unemployment*. Opinion surveys show that the vast majority of Europeans recognize the value of the existing machinery and wish to retain and improve it, recognizing that it is an *essential vector of social cohesion*.

The question is then: how can the positive aspects be consolidated while overcoming the negative effects? In order to help increase job opportunities, combat social exclusion and reduce the cost of unemployment, it has proved necessary to put in place an active employment policy which combines income support, professional training and tapping new sources of employment. How can social protection be made more conducive to this active employment policy? How can it be

¹² COM(95) 134, point 6.1.1.

integrated in employment promotion by relating for example the payment of benefit to active measures of economic integration of first-time job-hunters or the retraining of unemployed workers? How can it be ensured that social protection promotes integration into the labour market, i.e. that payment of benefits should not become a disincentive to legitimately remunerated work? And in this context, when benefits become more targeted on the most needy, because of financial pressures, how to avoid the problem that efforts made by recipients to get higher wages lead to very small changes in their disposable income?

Another aspect relates to the growth of part-time work, temporary work and teleworking, affecting women in particular. Unless full social protection rights are given to these workers, to what extent is there a perverse effect that an individual does not enjoy better rights when in work than when unemployed.

2.2 The financing of social protection

All the Member States are concerned about the financing of their social protection schemes. While revenue, which mostly comes from wages and salaries is at a standstill because of poor employment levels, expenditure is increasing, particularly as unemployment persists. It is not possible to sustain substantial deficits in the long term. Even in the short term, the present budget deficits contribute to the pressures on interest rates and consequently to the delay in economic recovery.

Member States appear to have limited scope to put up social charges and contributions levied on wages and salaries: they are seen as relatively high already in many countries. As a proportion of GDP, the tax burden on labour increased at Community level from 19% in 1980 to 21% in 1993.

There is now general agreement that the cost of low-skilled labour should be reduced, and as a consequence the magnitude of non-wage labour costs is seen as being too high. One of the five priorities of European employment policy set by the Essen European Council was reducing indirect labour costs, notably in relation to low pay.

In this context, a significant number of Member States are looking at ways to diversify sources of financing and examining how to obtain tax revenues for the financing of social protection. For example, some of them are beginning to attempt to shift the burden of taxation from employment to natural resources, with a view to discourage their excessive use. Other Member States are trying to tie benefits more closely to contributions. In any case, reforms of the structures of compulsory charges and contributions are in hand or in preparation in many Member States.

In this context of change, is there a need for closer Community cooperation on these matters between the Member States?

The design of the social protection system is also being examined in some Member States in terms of where the line is to be drawn between statutory and supplementary provision. In order to lower the rate of compulsory social contributions, some proposals are being made to reduce the former and give more importance to the latter. What would be the impact of such a change on distribution of incomes within societies, and what would be the consequent impact on the labour market? Is there a risk that wage discrepancies would be widened if they are associated with bigger differences, as far as social protection rights are concerned, between firms according to their size and activity? How can an adequate balance between statutory and supplementary protection be reached, which maintains social cohesion within Member States and meets the growing need for greater flexibility in modern economies?

2.3 The impact of demographic changes

The gradual progression of the baby boomers born after the war to working life and, after 2010 to retirement is now producing its first effects. This will play its part in intensifying ageing from the next century. The most recent UN forecasts on demography show that the total population in the 15 EU Member States will be more or less the same in 2020 as it is now. This assumption is based on estimates of lower fertility rates that EUROSTAT now consider to have been conservative, and it may be possible that by 2020 the European population will drop below today's levels. But what is sure is that the number of people aged 65 and over will grow by 23 million, from 52 to 75 million, or almost 45%¹³. Moreover, it seems unlikely that the growing imbalance in the age pyramid will be remedied by immigration.

The strain of achieving the transfer to those above retirement age and the burden imposed on the future generation of working-age will depend critically on the underlying growth of the European economies between now and then, and what happens to jobs. In recent years, the effective dependency ratio has risen substantially, not because of the ageing of the population but because of earlier retirement and increasing unemployment. Higher employment rates than currently achieved could offset the effect on the dependency ratio of the ageing of the population and make it easier to obtain the income transfer required. At the same time, some Member States are discussing changes in the way their pension system is financed, and in particular the balance between capitalization and pay as you go schemes. Is there a need to discuss the impact of such changes, for example on economic

¹³ The Commission produces an annual report on "The demographic situation in the European Union"; see COM(94) 595.

growth and job creation and the objective of maintaining solidarity between generations ?

The progressive transformation of family structures and lifestyle trends also makes it necessary to adapt existing schemes. Some of the systems are still implicitly based on a traditional family concept, in which the husband is the breadwinner while the wife has no paid activity, the two partners are linked by marriage, and that link is only broken with the death of a spouse.

It is well known that this is no longer the dominant model, with the very significant increase in the activity rate of women, the increased frequency of divorce, and the increasing proportion of unmarried couples and single-parent families.

Some social protection mechanisms, particularly those used for calculating pension rights, are ill-suited to meet these trends. Increasing consideration is given to individualization of rights and contributions. But the change in lifestyles and working practices also creates new social protection needs. This is the case, for example, with the care of elderly dependants, which is more and more difficult for adult children to provide on an informal basis. More generally, the traditional patterns of solidarity between generations are changing, and will increasingly be modified with the ageing of the populations.

2.4 Changes in health-care systems

The 1992 Recommendation on convergence set out a clear definition of the social protection policy objectives in this area: (i) to maintain and develop a high-quality health-care system geared to the evolving needs of the population, to the development of pathologies and therapies and the need to set up prevention; (ii) to ensure for all persons legally resident access to necessary health care as well as to facilities seeking to prevent illness.

Reconciling the twofold objective set out in the 1992 Recommendation with the constraint resulting from the need to keep public health-care expenditure under control is extremely difficult. Introducing market forces into the health-care sector has proved to be difficult, if one wants to avoid the adverse effects of risk selection. Whatever the way the system is organised, through sickness insurance or a national health service, detailed contracts or agreements between the providers of medical services, the paying bodies and the public authorities seem to be necessary. Given the complexity of these problems, exchanges of experience in this area would therefore be particularly useful. Moreover, closer co-operation between all concerned would now appear useful to identify the best solutions to the evolving needs of the population.

At European level, it would appear useful to analyze whether, as a first step, efficiency gains could be made by improving the complementarity in the supply of specialised health care across borders, and what administrative arrangements would be necessary. Could agreements be envisaged between the paying bodies to allow access where appropriate to the health-care system of another Member State?

2.5 Social protection and freedom of movement

There has been a substantial change in the nature of migration across the Union. Generally speaking, during the 60's and the 70's only workers and their families used their right to mobility. The current situation is very different: many non-active persons, whether retired or students, people undergoing training and job-seekers want to move to another Member State.

The increased importance of supplementary social protection has reduced the ability of coordination mechanisms to promote free movement of workers. There is currently no mechanism or arrangement dealing with the maintenance or transferability of supplementary old-age pension entitlements, for example. Given that these supplementary provisions will probably become increasingly important, the question arises of the extent of the obstacle this presents to the development of a European labour market.

Another problem for people using the right to free movement or free establishment is linked to the fact that the financing of social protection differs between Member States. Since there is no coordination between taxation legislation and applicable social security rules, - as already exists for social security contributions in Regulation 1408/71- this can lead to some problems for frontier workers, whether employed or self-employed. Some workers have to pay high levels of both taxes (in the country of residence) and social security contributions (in the country of work), and other ones take advantage of being in a symmetric position. Is there scope for closer coordination to help overcome these problems?

Directives governing the right of residence require people not to be dependent on the welfare system in the host country. This can, for example, make it difficult for someone who is unemployed in one Member State, to go to another Member State to look for work while continuing to receive unemployment benefits. The Commission has already presented a proposal to amend Regulation 1408/71 to help overcome this problem. More generally, is there a need to reflect on how the interpretation of this requirement - which is designed to avoid the risks of "benefit tourism" - can be reconciled with the right of free movement?

More generally, the question of the future evolution and scope of coordination of social protection systems between Member States is being raised. The aim of coordination is to promote free movement. Can coordination operate satisfactorily if the

Member States' social protection systems grow further apart or become increasingly complex, for example by the trend towards targeting and means-tested benefits? What are the main obstacles to simple and effective coordination and how can we overcome them? And what are the consequences of such wide differences from one country to another of key determinants of social protection, such as the conditions and age of retirement and the definition of incapacity for work?

2.6 Social protection and freedom to provide services

Collective social protection systems coexist with individual self insurance provision. People who can afford to do so often enter into private contractual arrangements to top-up benefits from collective schemes, both statutory and professional.

Collective systems are organised on the basis of pooling risks: everyone contributes, everyone benefits. The financial viability of the schemes depends on balancing the good risks with the bad. The good risks are those who are better qualified, in good health, in employment for example. The likelihood is that these people benefit less from the schemes than the other ones. If there is no compulsion for people who are good risks to belong to collective schemes, then the defined level of benefits could not be maintained.

There is a grey area as to the extent to which compulsory affiliation to schemes which are not statutory schemes is compatible with European law. Whilst the European Court of Justice will rule on such questions on a case by case or scheme by scheme basis, is there a need to explore what general principles should be applied with a view to achieving the Community objective of providing a high level of social protection and to avoid unbalancing schemes, and predetermining Member States' choices in this area?

2.7 Social protection in the longer term

Europe must achieve change if it is to be at the forefront of economic and technological progress. And, as emphasized in the Green¹⁴ and White¹⁵ Papers on European social policy, the Union is fully committed to ensuring that economic and social progress go hand in hand. A medium-term strategy is needed which will draw together economic and social policies in partnership rather than in conflict with each other.

The role of transfer and redistribution may become increasingly important in the future, since there has been a tendency in recent years towards a widening of income discrepancies, and consequently the risk of poverty and exclusion is increasing. In that context, social protection

¹⁴ COM(93) 551

¹⁵ COM(94) 333

systems will have to be adapted, not only because of the funding pressures but, more fundamentally, because of the need to move towards more active policies aimed at ensuring that everyone is integrated into work and society. Within the overall prospect of change, specific challenges will have to be addressed, such as how to promote the integration of the current generation of young people into the labour market and how to ensure that everyone has equal opportunities.

The 1992 Council Recommendation on convergence of social protection objectives and policies recalled that one of the basic objectives of social protection is to help to further the social integration of all persons legally resident within the territory of a Member State and the integration into the labour market of those who are in a position to exercise a gainful activity. The 1992 Recommendation on the guarantee of minimum resources defined the basic right of a person to sufficient resources and social assistance. The Commission will examine the efforts being made to meet these objectives. A link between the acknowledgment of this right and active measures for social and economic integration has been established and many innovative experiences are under way in Member States. Would it be useful to organize an exchange of views on the way social protection can be an effective tool for fighting against exclusion?

On the other hand, changes in life-cycle patterns are appearing, which may lead to modifying the traditional sequence of education, work and retirement periods. There is a long-term trend to reduce the duration of work and to increase training periods throughout working life. Working conditions will tend to become more flexible and mobility will continue to increase. Given these changes, the current way of acquiring rights to social protection - and especially the link to work - may need to be revisited.

Finally, the globalisation of the world economy and the increased need for competitiveness are likely to require continuing moderation in the growth of labour costs. In the future it will probably be more difficult to meet the financing requirements of social protection by raising employers' social contributions and charges. As a result, it will increasingly be clear to workers, who receive wages and pay social security contributions and taxes, that there is a trade-off between disposable income today and entitlement to benefits tomorrow. The level and financing of social protection are therefore likely to become more sensitive political issues in the future, especially as demand for protection against social risks is likely to continue to rise. A common reflection on these subjects can only be useful.

3. A NEW FRAMEWORK

Member States retain responsibility for attaining the common objectives set by the European Union in the field of social protection. They will continue to determine its personal and material scope, to define benefit levels and eligibility conditions and to organise the financing and administrative operation of their systems. In order to fulfil the underlying objective of social cohesion and solidarity, Member States will continue to adapt their systems so as to maintain or attain a high level of social protection.

Since it is responsible for freedom of movement for persons, freedom to provide services and competition, the Union does intervene indirectly in respect of social protection issues within those areas. It is important to ensure that social objectives are taken into account in these other areas. An integrated approach should be followed and there is an obvious value in setting in train common reflection on the future of social protection in the Union.

3.1 The aims

The Commission accordingly proposes that the Community institutions and the Member States should embark together on a process of common reflection on the future measures that should be taken to make social protection systems more employment-friendly and more efficient.

3.2 The means proposed

This common reflection must obviously be a collective process in which the Commission has a role to play as well as the Member States. The social partners and all the players concerned by social protection will be called upon to make their contributions. The European Parliament, the Economic and Social Committee and the Committee of the Regions must be fully associated in this reflection.

Drawing on the results of this process of common reflection, the Commission will take stock of reactions to this invitation to debate before the end of 1996, and propose appropriate follow up.

3.3 The role of the Commission

The Commission will initiate this process of reflection on the future of social protection in the Union, presenting to the Member States and the partners concerned analyses and orientations for debate. It is envisaged that the Member States and the others partners would also do this.

The Commission's main counterpart for dialogue will be the consultation group of Social Security Directors-General. Other consultation groups will also be used in both the employment and internal market areas. The European social

dialogue bodies will be requested to take an active part in the reflection.

3.4 Subjects for analysis and debate

Several issues would appear to be ripe for further analysis and common reflection, in particular:

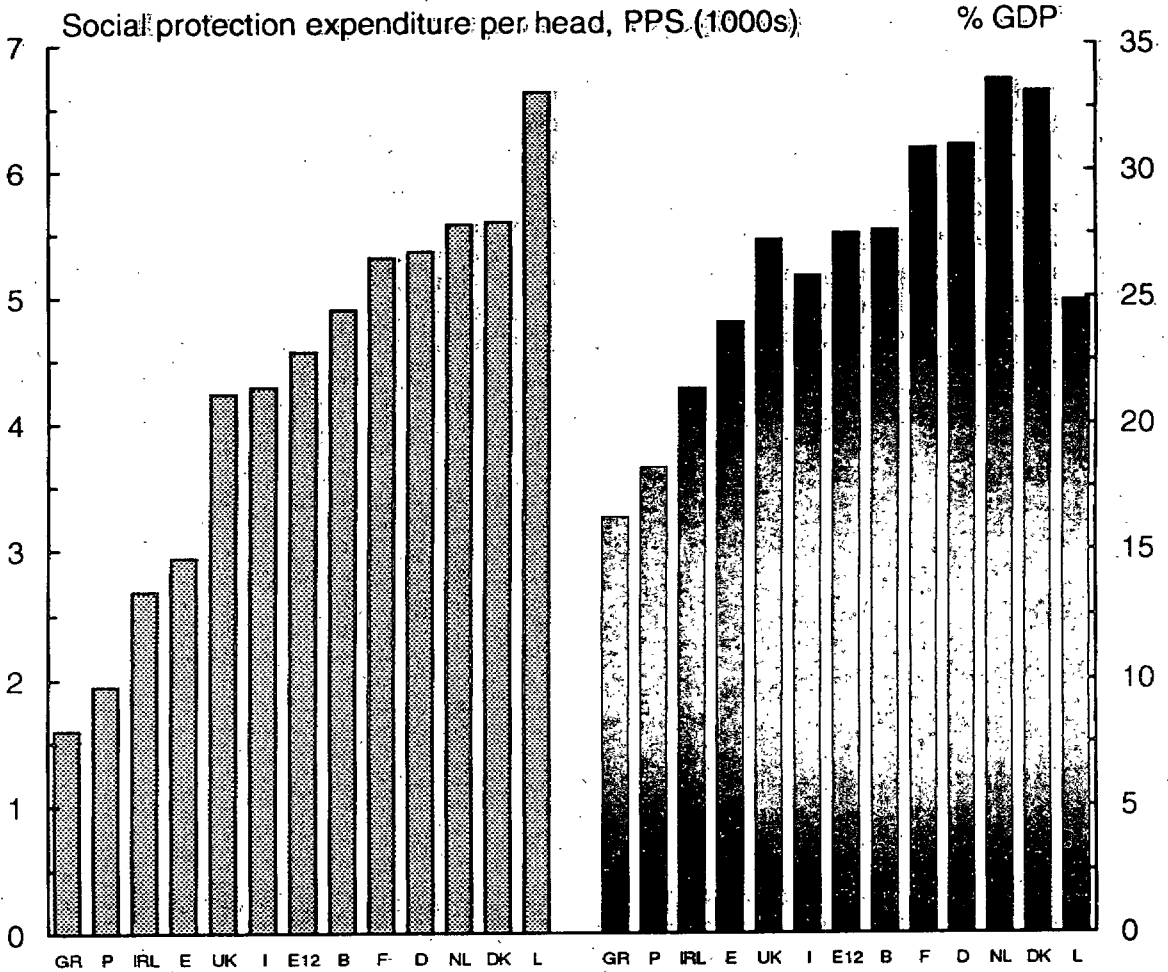
- the challenges arising from the deteriorating relationship between the size of the labour force and the numbers of pensioners;
- how to make social protection more employment-friendly;
- the financing of social protection;
- changes in health-care systems, notably the establishment of more systematic exchanges of experience in this field between the Member States;
- a broad assessment of the operation of the coordination of social security schemes for persons moving within the Union and examination of the relationship between coordination and convergence of social protection systems;
- a systematic examination of the principles whereby the institutions managing both statutory and supplementary schemes and insurance companies can operate alongside each other in the internal market;
- reflection on the future of social protection in the longer term.

4. CONCLUSION

The Commission calls upon the Council to:

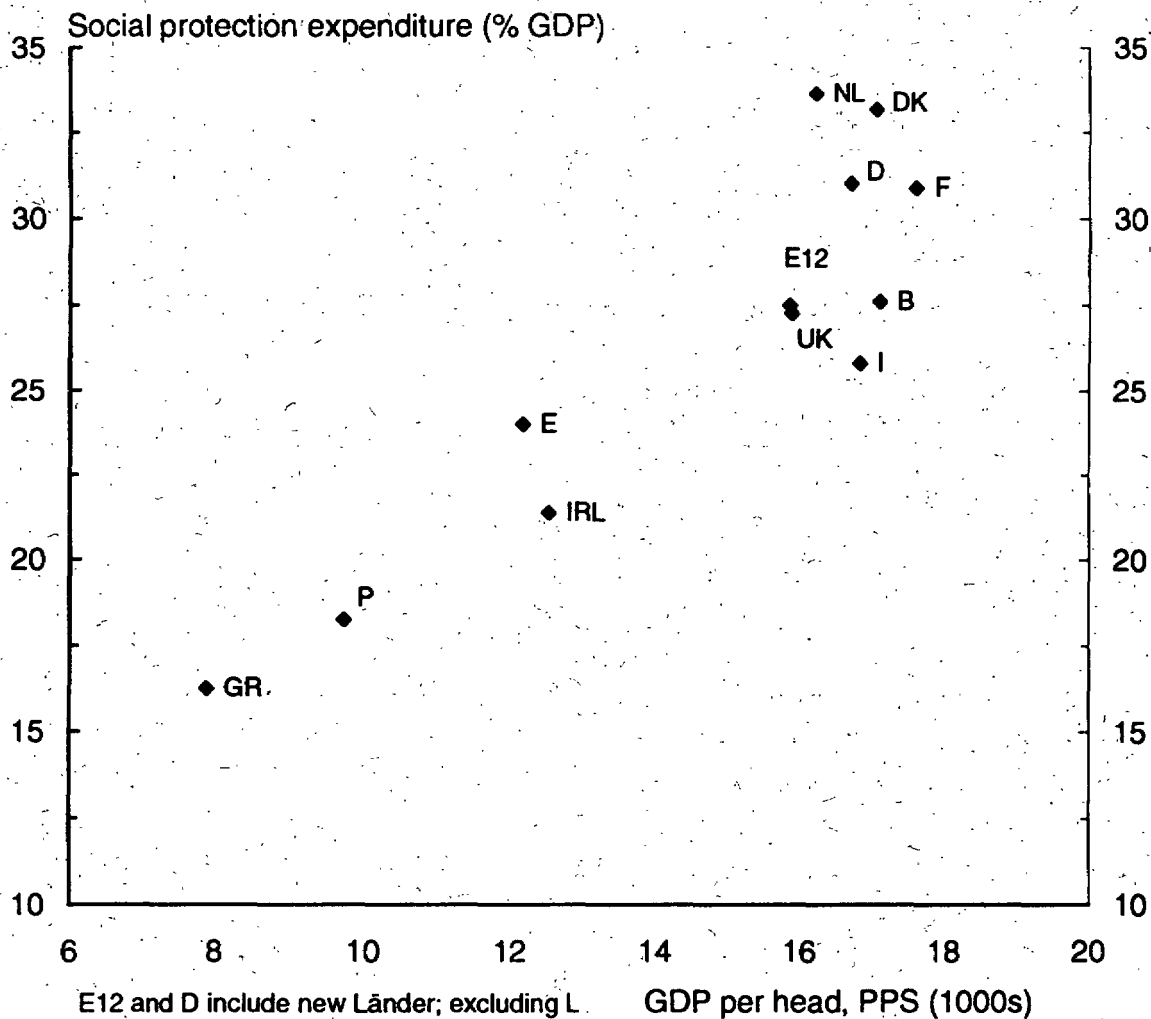
- acknowledge the importance of developing a framework for debate on the future of social protection in which the Member States and the Union could pool their efforts towards improving the workings of their social protection systems and make them more employment-friendly and more efficient;
- agree to associate all the players concerned at national and Community level, notably the social partners;
- take note of the Commission's intention to take stock of reactions to this invitation to debate before the end of 1996, and to propose appropriate follow up.

Social protection expenditure per head and in relation to GDP, 1993

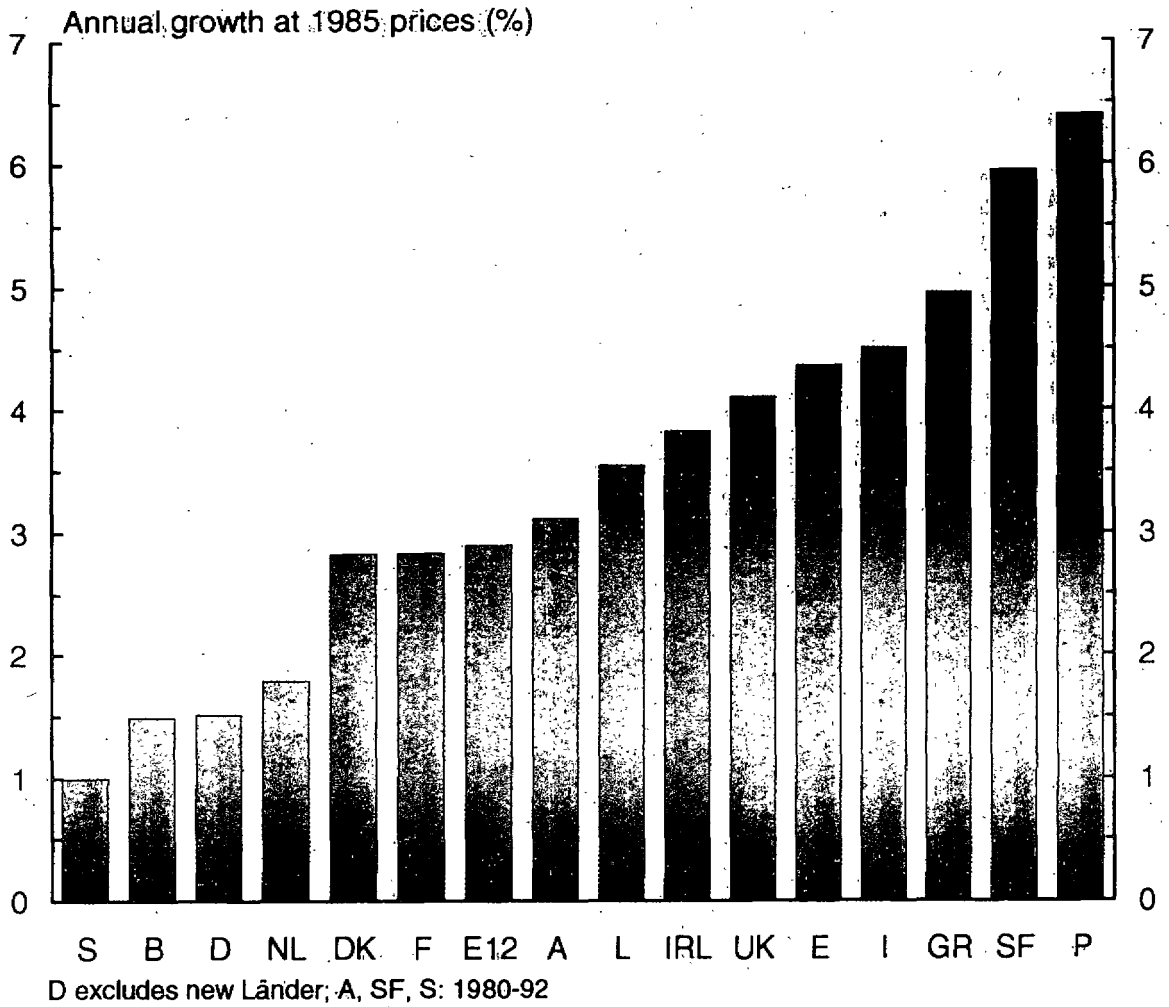


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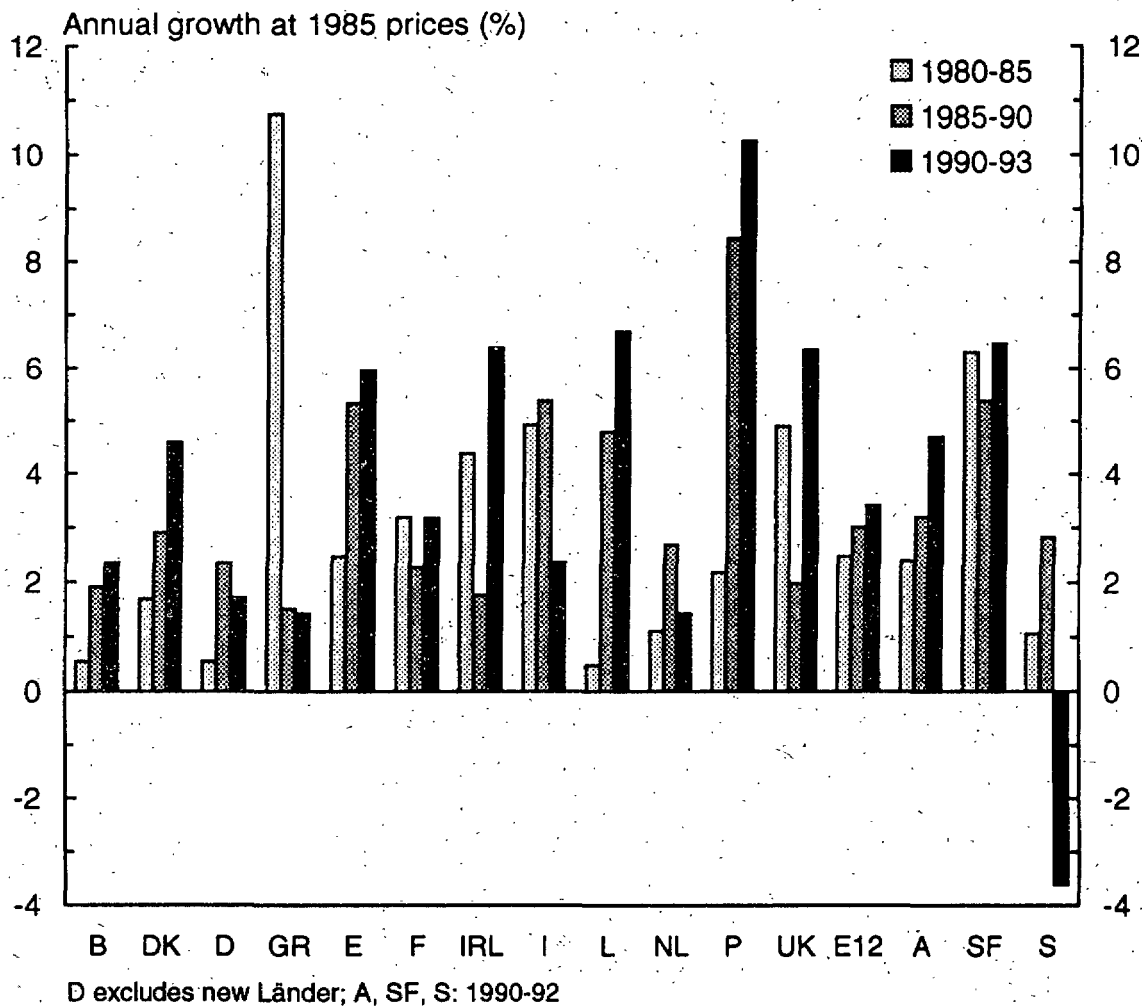
Social protection expenditure and GDP per head, 1993



Growth in expenditure on social protection benefits per head, 1980-93



Growth in expenditure on social protection benefits per head, 1980-85, 1985-90 and 1990-93



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