How much do OECD countries spend on social protection and how redistributive are their tax/benefit systems?

Willem Adema, Pauline Fron and Maxime Ladaique

Organisation for Economic Co-operation and Development, Paris, France

Abstract The global economic crisis has reignited interest in social policy and public spending on different types of social benefits. Public social spending-to-GDP ratios are often used to consider the magnitude of welfare systems in international perspective, but such comparisons alone give an incomplete picture of social effort across countries. This article looks at these different factors, before briefly considering the redistributive nature of tax/benefit systems in different member countries of the Organisation for Economic Co-operation and Development (OECD). The article also considers trends in social spending and compares spending in the late 2000s with the early 1990s when the previous economic crisis played out. The article ends by illustrating the profound effect the recent global economic crisis had on social spending trends across OECD countries.

Keywords income redistribution, benefit, taxation, welfare state, public-private mix, economic crisis, OECD

Addresses for correspondence: Willem Adema (Willem.ADEMA@oecd.org), Pauline Fron (Pauline.FRON@oecd.org) and Maxime Ladaique (Maxime.LADAIQUE@oecd.org), Social Policy Division, Organisation for Economic Co-operation and Development, OECD Headquarters, 2 rue André Pascal, 75116 Paris, France <http://www.oecd.org/els/social>. The authors are grateful to Michael Förster, Horacio Levy, Monika Queisser, Laura Quintin and two anonymous reviewers for comments on a previous draft. The views expressed in this article cannot be attributed to the OECD or its member governments; they are the responsibility of the authors alone.
Introduction

Over the last five decades, public social spending across the member countries of the Organisation for Economic Co-operation and Development (OECD) has more than doubled from 8 per cent of GDP in 1960 to 22 per cent in 2013 (OECD, 2013a). However, the increase in the OECD average masks considerable differences in individual country experiences. Figure 1 shows that, in 2013, continental European and Nordic welfare states were among the most comprehensive welfare states across the OECD, with public social expenditure-to-GDP ratios being more than 30 per cent of GDP in Belgium, Denmark and France, while at the other end of the scale public spending is 10 per cent of GDP or less in Chile, Republic of Korea and Mexico.

These differences are in part related to the stage of socio-economic development. Many Western and Northern European countries started to develop their welfare systems in earnest in the 1960s and 1970s, by introducing and increasing

Figure 1. Public social expenditure in percentage of GDP in 2013\(^1\)\(^2\)\(^3\)

Notes:
1. Estimates for 2013, see note 1 to Figure 5.
3. The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

the generosity of different social programmes (ranging from maternity leave to support for the frail elderly), while economies such as the Republic of Korea, Mexico and Turkey began to develop their social systems more recently.

As they help shape the demand for health services and provisions in retirement, differences in age structures of populations also contribute to cross-national spending differences (see Figure 1). For example, Mexico and Turkey are the two youngest OECD countries to have high “old-age support ratios” with nine or more people of working age (20–64) per senior citizen (OECD, 2011a), which helps explain why they are at the bottom of the public social spending rankings across OECD countries. By contrast, Belgium, Germany and Sweden have below average old-age support ratios (as well as relatively generous benefits with high coverage among senior citizens), which contribute to high public social spending in international comparison.

Policy choices on the design of welfare provisions also affect public spending-to-GDP ratio across countries. Welfare states with a greater focus on social insurance and earnings-related benefit payments (e.g. France and Germany) involve more social spending than systems which have a greater focus on income-tested social support, e.g. Australia and the United States.

Furthermore, public spending data, as in Figure 1, do not cast light on the extent to which countries provide social support through the tax system, (e.g. France, Germany and the United States) or levy direct tax on benefit income and/or indirect tax on consumption out of such benefit income, and such tax flows are particularly important among comprehensive welfare states such as Denmark and Sweden. Figure 1 also does not illustrate the important differences in the role of the private sector in the provision of social support, which often concerns collective pensions (e.g. the Netherlands and Switzerland) or collective health insurance through employer-sponsored plans as in the United States.

This article first considers different factors that affect international comparisons of social spending including the stage of the business cycle and the more structural role of health and pension spending, cross-national differences in the role of private social expenditure, and the extent to which countries’ tax systems affect social spending. These factors and a welfare state’s focus on social insurance or earnings-related benefit payments rather than income-tested support affects the redistributive power of welfare states, which is discussed in the subsequent section. The article concludes by illustrating recent social spending trends. It shows that, at least initially, policy in many OECD countries tried to cushion the

1. A comprehensive view of social protection policy includes an assessment of social spending, the adequacy of social benefits and their coverage among the population. However, such a wide-ranging study is beyond the purview of this article.
impact of the crisis on disposable household income by sustaining public social spending, but that more recently the focus has shifted towards possible benefit cuts, at least in real terms, to curtail public social spending.

Issues in comparing public social spending across countries and over time

Comparing social spending across broad spending categories in 2009 with a year that reflects a similar stage in the business cycle facilitates looking at spending on income support benefits in times of economic downturns, but also at the structural drivers of spending trends. To start with the former, Figure 2, Panel B shows that in about half of the 27 OECD countries for which time series are available from at least 1990 onwards (see the notes to Figure 2), public spending on income support to the working-age population as a per cent of GDP was higher in 1991/92 than currently, and the differences are most pronounced in the Netherlands, Poland and the Scandinavian countries. In particular, the Finnish, Polish and Swedish economies were affected by the break-up of the Soviet Union in the early 1990s. Also, the Netherlands and Sweden were the only two OECD countries where GDP growth outpaced social spending growth over the 1990–2012 period (Adema, Fron and Ladaique, 2011). This was partially because of tightening access conditions to disability benefits and making employers responsible for continued payment of (part of the) wages during the initial period of absence from work due to sickness (see below).

Figure 2, Panels A and C illustrate that ageing populations (OECD, 2011a) and maturing pensions systems (OECD, 2011b) structurally drive up pension and health expenditures. In 2009, public pension expenditure amounted to 7.8 per cent of GDP, up from 6.7 per cent in 1992, with increases by 4 percentage points of GDP or more in Italy, Japan, Portugal and Turkey. Over the same period, public health spending grew from 5.2 to 6.8 per cent of GDP, with growth by 3 percentage points of GDP or more in Portugal and Turkey. Only in the Netherlands and New Zealand did GDP growth outpace public pension spending: in the Netherlands access to early retirement and survivor pensions has been tightened since the early 1990s, while in New Zealand the growth in pension spending was curtailed by the gradual increase of the retirement age from 60 to 65 over the 1992–2001 period (MSD, 2013).

With the global financial crisis, increases in public health spending halted in 2010 (Morgan and Astolfi, 2013), while the crisis often also provided added impetus for reforms needed to ensure the financial sustainability of pension systems (OECD, 2011b and 2012a). In particular, many countries gradually phased in increased retirement ages – as New Zealand did during the 1990s. Such reforms
Figure 2. Public social expenditure by broad spending category as a per cent of GDP, early 1990s and 2009: Public spending on pensions, income support to the working-age population, health and other social services

2A. Cash benefits: Cash pensions, old age and survivors

2B. Cash benefits: Income support to those of working age

Notes:
1. There are two main criteria which both have to be satisfied for an expenditure item to be classified as social: i) the OECD considers nine policy areas: old-age, survivors, incapacity-related benefits, health, family, active labour market benefits, unemployment, housing and other social policy; and, ii) participation in a programme has to be compulsory and/or involve inter-personal redistribution of resources; see Adema et al. (2011).
2. Figure 2 groups social spending in four broad spending categories: Pensions (old-age and survivors cash benefits), Income support to the working-age population (cash benefits concerning sickness, disability, family, unemployment, housing and other income supports) (e.g. social assistance payments); Health services and other services (services to the elderly and disabled, family services (including childcare)), and other social services. In contrast to Figure 1, spending on Active Labour Market Programmes (ALMPs) is not included here as it cannot be cleanly split into cash and service spending. OECD average does not include Chile, the Czech Republic, Estonia, and Hungary for which data for the early 1990s were not available.
Notes: (continued)

Source: OECD (2013a), Social Expenditure Database (SOCX) <www.oecd.org/els/social/expenditure>
are unlikely to deliver immediate reductions in social spending, but it illustrates that the crisis has put further focus on the need to reform social welfare systems to cope with ageing and the resulting structural upward pressure on social spending.

Considering Figure 2, Panels A and B together vis-à-vis Panels C and D, it appears that in 2009 countries on average spent more on cash benefits (12.6 per cent of GDP) than on health and other social services (9.0 per cent of GDP). Figure 2 also suggests that income support to the working-age population is the one area where on average across the OECD public spending has not increased, whereas the relative importance of in-kind social spending has grown over the last 20 years. In particular, Canada, the Netherlands, New Zealand, the United Kingdom and the Nordic countries had the most equal balance in spending on cash and in-kind benefits. Low-spending countries like the Republic of Korea and Mexico had a greater focus on services in social support.

**Private social expenditures**

International comparisons of social spending are also affected by differences in the extent to which societies stimulate and/or rely on private actors to take out social protection arrangements outside the public sector. All social spending with financial flows controlled by different levels of government and social security funds is considered as public. All other social benefits are considered as private, and from time to time benefits are rather similar. For example, sickness benefits financed by compulsory employer and employee contributions (receipts) to social insurance funds are by convention considered public. However, sickness payments directly paid by employers to their absent employees (as may be legislated by public authorities – see the Dutch and Swedish examples above), are considered as private social expenditure. Private social expenditure includes benefits provided by NGOs, benefits accruing from tax advantaged individual plans and collective (often employment-related) support arrangements, such as for example, pensions, childcare support, and private health insurance. Out-of-pocket expenditure on health services is not included in private social expenditure.

Private social expenditure amounted to 3.2 per cent in 2009 on average across the OECD (for countries for which data are available), up from 2.3 per cent in 1991 (Figure 3). Private social spending was highest at over 10 per cent of GDP in the United States, while it accounted for around 5 per cent of GDP in Canada, Iceland, the Netherlands and the United Kingdom. Private social spending accounted for less than 1 per cent of GDP in about one quarter of OECD countries.

Private social benefits often involve benefits prescribed under occupational accidents and diseases legislation (e.g. Australia), sickness benefits (e.g. Germany) and old-age pensions. Private pension plans involve mandatory and voluntary
employer-based programmes (e.g. Switzerland and the United Kingdom), or tax-supported individual pension plans (e.g. the United States); private pension benefit payments exceed 3 per cent of GDP in Canada, Iceland, Japan, the Netherlands, the United Kingdom and the United States. Private social health expenditure exists in most countries, but it is nowhere near as important as in the United States, where employment-related health plans are widespread and contributed to private social health spending amounting to 6.1 per cent of GDP in 2009.

The role of tax systems

Tax systems also significantly affect social spending and international comparisons of social effort. This is because there are significant differences across countries in the extent to which governments affect the “real” level of social spending by: i) levying direct income tax on benefit income; ii) imposing indirect taxation on

Figure 3. Private social expenditure in percentage of GDP, early 1990s and 2009

Note: Early 1990s data refer to 1993, but concern 1991 for Australia, Canada, Finland, Ireland, New Zealand, Switzerland, United Kingdom and United States; 1992 for Iceland, Rep. of Korea and Luxembourg; 1995 for Slovakia; and, 1996 for Slovenia. Data refer to 2009 except for Switzerland 2008. The OECD average does not include Chile, Czech Republic, Estonia, Hungary, Luxembourg and Poland as data for early 90s were not available. By convention the System of Health Accounts (OECD, 2011c) classifies expenditure through mandatory health insurance systems in the Netherlands and Switzerland as public, and relevant amounts have been included in Figure 1.

consumption out of benefit income; and/or, iii) pursuing social policy goals through the tax system by means of tax breaks with a social purpose.

First, governments levy direct income tax and social security contributions on cash transfers to beneficiaries. In fact, in some countries almost all public cash transfers are taxed, as for example, in Denmark or Sweden, while in other countries benefits are frequently paid net of tax, as for example, in the Czech Republic, Slovakia and Anglophone welfare states which have a greater focus on means-testing in the payment of cash transfers. Similarly, taxation of benefit income also varies across benefits: child allowances, unemployment assistance, social assistance, and rent support benefits are often not taxed, while disability and old-age pensions can be taxed at a reduced rate while continued wage payments in case of absence due to sickness are often taxed in the same way as earnings.

Figure 4, Panel A shows that in Denmark and Sweden direct taxation of public benefit income amounted to more than 3 per cent of GDP in 2009, while this was less than 0.5 per cent of GDP in Anglophone countries, the Czech Republic, Slovakia, the Republic of Korea and Mexico. Pension payments accruing from collective or individual pension savings is taxed at a higher rate than income-tested payments. This underlies the large share of direct taxation levied on private transfers relative to direct tax on public benefits in Australia, Canada, Iceland, the Netherlands, the United Kingdom and the United States.

Second, benefit income is provided to finance consumption of goods and services, on which governments levy indirect taxation. This matters for international comparisons because in countries with lower indirect tax rates it requires lower benefit payments, and thus less gross (before tax) social spending, to achieve the same amount of social support.2

Figure 4, Panel B shows that tax rates on consumption are often considerably lower in non-European OECD countries than in Europe. Indeed, indirect tax of consumption out of benefit income is generally worth less than 1 per cent of GDP in non-European OECD countries. In Europe, tax receipt out of consumption of benefit income is lowest in Slovakia and Spain at about 1.5 per cent of GDP and highest in Austria, Denmark and Luxembourg at around 3 per cent of GDP.

Third, in addition to tax reductions on particular sources of benefit income (which are captured by the variation of direct taxation of benefit income discussed above), governments pursue social policy objectives by means of Tax Breaks with a

2. Indirect taxes play an important role in the economy and since 1995 consumption taxes constitute about 10 to 11 per cent of GDP (OECD, 2012b). Over the 2007–2013 period, standard value added tax (VAT) rates increased in about half of the OECD countries, but over this period overall tax revenue from goods and services as a per cent of GDP remained essentially unchanged on average across the OECD (LeBlanc, Matthews and Melbye, 2013). To what extent calls for a rationalization of tax systems and a more uniform VAT system (Mirrlees et al., 2011) will affect the balance of direct and indirect tax revenue remains to be seen.
How much do OECD countries spend on social protection and how redistributive are their tax/benefit systems?

Figure 4. The tax system and social spending

4A. Direct taxes paid by recipients of public/private benefits, in percentage of GDP, in 2009

4B. Indirect taxes paid by recipients of public/private benefits, in percentage of GDP, in 2009
Social Purpose (TBSP). These are defined as: “... those reductions, exemptions, deductions or postponements of taxes, which: a) perform the same policy function as transfer payments which, if they existed, would be classified as social expenditures; or b) are aimed at stimulating private provision of benefits...” (Adema, Fron and Ladaique, 2011).

Figure 4, Panel C shows that fiscal support similar to cash benefits is important in France, Germany, Mexico, the United Kingdom and the United States. TBSPs similar to cash often concern support for families. For example, the value of support to children in France through the *quotient familial* was around EUR 10.1 billion in 2009 (OECD, 2013a). Portugal uses tax breaks towards a range of social purposes: health tax credits to household spending on health services; child tax credits; housing credits and tax credits for the disabled; housing for the elderly; and for carers with low-incomes providing services to elderly relatives.

Sometimes, fiscal support and cash transfers for families are an integral part of the same social programme, with cash payments recorded in the *OECD Social Expenditure database* and fiscal support in the *OECD Revenue Statistics* (OECD, 2012b). For example, in Germany in 2009 tax relief for children amounted to EUR 38.5 billion, of which EUR 23.1 billion was off-set against tax liabilities (and thus recorded as a TBSP) and EUR 15.4 billion paid out in transfer income, and thus...
recorded as a cash transfer. To ensure that low-income households can take full advantage of relevant tax supports some tax programmes with a social purpose concern “non-wastable” or “refundable” tax credits.3 With the financial crisis the number of low-income households and families has increased and so has public spending on these programmes. In the United Kingdom, spending on the Child Tax Credit and the Working Tax Credits jumped up by one third in two years from GBP 19.5 billion in 2007 to GBP 26.8 billion in 2009.4 Similarly, in the United States spending on the Earned Income Tax Credit jumped up from USD 48.5 billion in 2007 to 59.2 billion in 2009 and most of this was due to cash payments (USD 54 billion) rather than tax credits that mirror cash benefits. The Mexican Subsidio para el empleo is another hybrid of tax and cash support. Employers make payments in conjunction with wages to eligible low-income workers increasing their take-home pay; the employer then offsets these payments against his/her tax liabilities.

Governments sometimes also use the tax system to support the provision of social services by NGOs or stimulate takeup of private social insurance coverage by individuals and/or employment-related plans. These tax breaks can be categorized in two broad groups. First, there are “Tax breaks towards current private social benefits”, i.e. favourable tax treatment aimed at stimulating the provision of private social benefits in the current year such as private health insurance. This type of tax break is important in Canada,5 Germany and particularly in the United States, where the exclusion of employer contributions for medical insurance premiums and medical care (including for the self-employed) amounted to almost USD 150 billion in 2009, equivalent to 1.0 per cent of GDP. Tax breaks towards current private social benefits also include favourable treatment of contributions to and the income of NGOs. Again this form of fiscal support is most prevalent in the United States where deductibility of contributions to charities other than education or health amounted to USD 36.7 billion in 2009, or 0.3 per cent of GDP.

The second group of tax breaks towards private benefits are those towards pensions. However, estimating the value of tax breaks for pensions is complex as favourable fiscal treatment can occur at three stages of pension saving: when

3. In case of a “wastable” (or “non-refundable”) tax credit, entitlements only accrue to the extent that they are off-set against tax liabilities, while “non-wastable” or “refundable” tax credits involve cash transfers to people (e.g. low-income workers) whose tax liabilities are not large enough to make (full) use of a particular entitlement (tax credit). Non-wastable tax credits thus reinforce the redistributive nature of a tax/benefit system.
4. In the United Kingdom in 2009, GBP 1.6 billion spent under the Working Tax Credit was recorded as a TBSP, while GBP 6.2 billion concerned cash payments; similarly under the Child Tax Credit programme GBP 3.8 billion was recorded as tax support whereas GBP 15.2 billion was paid out in cash.
5. The available data on TBSPs for Canada underestimate their overall value as data on fiscal support with a social purpose by provincial authorities is not available on a comprehensive basis.
contributions are made; when capital income is generated; and when pensions are paid out. Estimation methods are not standardized across countries and, therefore, the data that is available on the cost to public budgets of tax relief to private pension plans is not directly comparable across countries and not included here in the overall calculations of net (after tax) social expenditure. However, available information for 2009 shows that the value of favourable tax treatment of private pension arrangements can be substantial and was in excess of 1 per cent of GDP in Australia, Canada, Iceland, Ireland, Israel, the Netherlands, Switzerland and the United Kingdom. These are also the countries where private pension saving is most important (OECD, 2012a).

From gross public to net total social expenditure

Pulling together information on public and private social expenditure as well as the impact of the tax system gives a more comprehensive view of social spending across countries. Subtracting the value of direct and indirect taxation of benefit income of gross public social expenditure (see line 1 in Table 1), while adding the value of Tax Breaks with a Social Purpose gives an indicator of net current public social expenditure (line 2). This indicator gives an impression of the real magnitude of budgetary efforts in the social field. Also, considering information on private social spending (line 3) and taxation of such benefit income (line 4) identifies that proportion of an economy’s domestic production to which recipients of social benefits can lay claim: net total (public and private) social expenditure (line 5).

Going from gross public to net total social expenditure (Table 1), the following findings emerge:

• Both gross and net public social spending are highest in France and lowest in Mexico, but the difference between maximum and minimum public social spending-to-GDP ratios across the OECD is somewhat reduced: by about 2 percentage points of GDP.

• In most countries, governments claw back more money through direct and indirect taxation of public transfer income than they award in tax advantages for social purposes. After accounting for the tax system, public social spending on average across the OECD is 2.4 per cent of GDP (or about 10 per cent of public social spending) lower than before. The effect of tax systems varies considerably across countries. For example, in Denmark and Sweden net public social spending is around 20 to 25 per cent below gross spending levels, while with 10 per cent of spending the adjustment in France is around the OECD average. This is because direct taxation of benefit income in France is around the OECD average, while French policy also makes intensive use of fiscal supports for families. By contrast, in the Republic of Korea, Mexico and in particular the United States, gross public spending is lower than net public spending, because benefit income is taxed at very
low rates, while the tax system is used relatively intensively to deliver social support directly or indirectly to subsidise its private provision.

- Considering both information on public and private social benefits and the importance of tax systems facilitates comparisons of net total social expenditure. This proportion is highest at 32 per cent of GDP in France. In Austria, Belgium, the Czech Republic, Denmark, Germany, Italy, Japan, Portugal, Spain, Sweden, the United Kingdom and the United States households lay claim to between 25 and 30 per cent of social expenditure. There is greater similarity in net total than gross public spending levels. This similarity is due to including private social spending (particularly in the United Kingdom and the United States) and the relatively high

Table 1. From gross (before tax) public to total net (after tax) social spending, in percentage of GDP at market prices, 2009\(^1,2\) (countries 1 to 15)

<table>
<thead>
<tr>
<th>Country ranking in term of Gross public social expenditure</th>
<th>1</th>
<th>2</th>
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<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
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<th>12</th>
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<td>29.0</td>
<td>27.8</td>
<td>27.8</td>
<td>26.0</td>
<td>25.5</td>
<td>24.5</td>
<td>23.9</td>
<td>23.5</td>
<td>23.1</td>
<td>23.0</td>
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<td>2.6</td>
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<td>0.9</td>
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<tr>
<td>+ TBSP (cash benefits towards vol private)</td>
<td>1.2</td>
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<td>0.0</td>
<td>0.1</td>
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<td>1.6</td>
<td>1.9</td>
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<td>0.5</td>
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<td>1.9</td>
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<tr>
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<td>25.4</td>
<td>26.3</td>
<td>28.1</td>
<td>24.8</td>
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How much do OECD countries spend on social protection and how redistributive are their tax/benefit systems?

Table 1. Continued (countries 16 to 30)

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<tr>
<th>Country</th>
<th>Ranking</th>
<th>Gross public social expenditure</th>
<th>Direct taxes and social contributions</th>
<th>Indirect taxes (on cash benefits)</th>
<th>TBSP (cash benefits towards vol/private)</th>
<th>Net current social expenditure</th>
<th>Gross private social expenditure</th>
<th>Direct tax</th>
<th>Indirect tax</th>
<th>Net current private social expenditure</th>
<th>Net total social expenditure (2+4)</th>
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<td>22.4</td>
<td>0.0</td>
<td>2.9</td>
<td>0.8</td>
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<td>22.2</td>
<td>0.7</td>
<td>0.7</td>
<td>0.6</td>
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Notes:
1. The figure in brackets refers to the ranking of countries in terms of gross public social expenditure from number 1 being the highest spender to the lowest; for example, the United States ranks 23rd in OECD in terms of gross public social expenditure. Data for Canada, Iceland, Luxembourg and Mexico have been estimated using data on direct tax rates of benefit income for 2007. In the absence of information on direct taxation of benefit income in Slovenia, total net social spending is overestimated for this country, and it is not included in the OECD average. Data for Israel concern public social spending only.
2. TBSPs include the value of TBSPs similar to cash benefits and TBSPs towards private social benefits (except pensions). However, in order to avoid double counting, the value of TBSPs towards private social benefits has been ignored for the calculation of net total social expenditure TBSPs.


level of direct and indirect taxation on income transfers and ensuing consumption in European countries vis-à-vis non-European countries.

• Moving from gross public to net total social expenditure also changes the ranking among countries (see italics in top and bottom rows in Table 1). Denmark, Finland, Luxembourg and Poland drop seven places or more in the rankings and
all of these countries tax benefits and associated consumption are above the OECD average. By contrast, Canada, the United Kingdom and the United States move up the rankings by seven or more places. In all of these countries private social spending is important while direct and indirect taxation of benefit income is below the OECD average. As private social spending is so much larger in the United States compared with other countries its inclusion moves the United States from twenty-third to second place when comparing net total social spending across countries.

**The redistributive power of tax/benefit systems**

Tax systems do not just affect levels of social spending; they also play a key role in the financing of social benefits, and thereby also affect the degree of redistribution in tax/benefit systems. The latter is related to the cross-national differences in the manner in which social programmes are financed through income tax, social security contributions, payroll taxes, indirect taxation or other general tax revenue (OECD, 2012b). For example, income tax systems often involve a degree of progressivity, while indirect taxation does not. Also, social benefit payments related to contributory records are less likely to redistribute resources than income-tested programmes (see, for example, Adema, Fron and Ladaique, 2011, Table I.1). The overall level of the tax burden, the degree of progressivity in tax systems, the degree of targeting within social programmes, and the level of social expenditure all help to determine the redistributitional nature of welfare states.

Considering the effect of tax and public cash transfer systems, rather than social expenditure levels, is a better, though imperfect (see below), way of looking at the redistribution of resources in societies (OECD, 2008). Table 2 gives a measure of the incidence of taxes and transfers in household income, with a focus on the bottom income quintile, and the redistributive effect through public cash transfers and taxes. It separately identifies the role of gross public transfers (the first three columns) and then taxes and social security contributions (the second three columns). The role of cash transfers in supporting the income of people in the bottom quintile is computed by first estimating the average ratio of cash transfers as a percentage of household disposable income measured in income surveys (column A); second, by calculating how much of this share goes to the poorest 20 per cent of the population (column B); and finally, by multiplying the size of spending by the progressivity of its distribution to calculate gross benefits accruing to people at the lower end of the distribution (divided by 100, in column C). The same procedure is used to calculate how much tax is paid by people at the lower end of the distribution (not including indirect taxation).

---

6. The bottom quintile covers different income shares in different countries: for example, the bottom quintile in Mexico gets 4 per cent of total income while in Denmark this is around 10 per cent.
### Table 2. The incidence of cash transfers and income taxes in household income and extent of overall redistribution among the population

<table>
<thead>
<tr>
<th></th>
<th>Gross public transfers paid to households</th>
<th>Direct taxes and social security contributions paid by households</th>
<th>Redistributive effect</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>A. Average ratio of household disposable income</td>
<td>B. Share of public transfers paid to lowest quintile (A*B/100)</td>
<td>C. Transfers to lowest quintile (D/E/100)</td>
</tr>
<tr>
<td>Australia</td>
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<td>Poland</td>
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The overall redistributive effect of public cash transfers and taxes to and from households is given by column H, which represents the difference between the Gini coefficients of market income and disposable income for 2010. The percentage reduction of income inequality (as measured by these Ginis) is also given for 2000. Thus, for example, in Australia average transfer income by households is about half of what it is across the OECD (column A), but spending is much more targeted on low-income families than in many other countries as over 40 per cent of transfer income – twice the OECD average – goes towards the poorest 20 per cent of the population (column B).\(^7\) Considering the tax system gives a mirror image for Australia: taxation per household is considerably lower than across the OECD.

\(^7\) For Australia, transfers paid to households do not include superannuation pension payments while taxes and social security contributions reported in Table 2 do not include superannuation contributions.

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### Table 2. Continued

<table>
<thead>
<tr>
<th></th>
<th>Gross public transfers paid to households</th>
<th>Direct taxes and social security contributions paid by households</th>
<th>Redistributive effect</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>A. Average ratio of household disposable income</td>
<td>B. Share of public transfers paid to lowest quintile</td>
<td>C. Transfers to lowest quintile (A*B/100)</td>
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</table>

Note: n.a.: Data not available.

OECD (column D) and income tax paid by the bottom income quintile is the lowest in the OECD (column E). The per cent difference between the Gini coefficient of market income and disposable income has diminished during the 2000s (column H). On the whole the redistributive power of the system of taxes and transfers in Australia seems to have weakened somewhat since the turn of the millennium.

In a cross-national perspective, Table 2 suggests:

- Column A shows that in Chile, Republic of Korea and Mexico public spending on transfers constitutes less than 10 per cent of average disposable household income; by contrast transfer income makes up over a third of average disposable household income in Austria, Hungary, Ireland and Italy.
- More than a third of transfer income is targeted at the bottom quintile in Australia, Denmark and New Zealand.
- Average taxation per household is on average one third of disposable household income or more, in Austria, Denmark, Iceland, Italy, the Netherlands, Norway and Switzerland.8
- Anglophone countries impose a limited tax burden on low-income families (column E) in contrast to Denmark, Iceland, Luxembourg, Poland, Slovakia and Switzerland (see above).

On the whole, the combined effect of public spending on cash transfers, and the targeted nature of benefit programmes and tax systems and the progressivity therein generates the largest redistributive effect amount of redistribution in welfare systems in Belgium, Finland, Hungary, Ireland and Slovenia (column H). These countries also rank among the countries with the lowest degree of income inequality (column G) and after tax poverty rates (OECD, 2013b). Table 2 does, however, underestimate the redistribution of societal resources, particularly in Denmark and Sweden, as it does not capture the redistributive effects of social service provision financed out of general taxation (and Figure 3 showed that both of these countries spend much more on public social services for the elderly, and early childhood care and education facilities for families of working age than most other OECD countries). Also, the results in Table 2 are static and do not capture behavioural effects nor do they present information on the possible redistributive nature of private social support.9

8. Data for Finland and Switzerland include pension contributions to (occupational) private pension funds which makes these numbers difficult to compare with the results for the other countries.
9. In the absence of data on a cross-national basis, Table 2 does not capture the redistributive effects of private social benefits. Some such benefits, e.g. social services provided by NGOs, will involve a higher degree of redistribution than earnings-related social insurance benefits. But many private programmes will generate less redistribution of resources than public programmes. Private employment-related social benefits mostly re-allocate income between the (formerly) employed population, and the same holds true for fiscally-advantaged individuals or group retirement plans: tax-advantaged programmes are more likely than not to benefit the most well-to-do (Adema and Whiteford, 2010).
Table 2 is somewhat ambiguous with respect to trends in the redistributive nature of tax and transfer systems since 2000. In some countries tax and transfer systems have become more redistributive (Belgium, Hungary, Italy, Japan, Portugal and the United Kingdom), while opposite trends were recorded for Australia, the Czech Republic, Denmark, Israel and Sweden (the redistributive effect of the Dutch system of taxes and transfers weakened during the 1990s).

**Social spending during the recent crisis**

OECD (2012c) showed that in the past public social spending-to-GDP ratios across the OECD generally increased with economic crises but only declined slowly afterwards, if at all. On average across the OECD, public social spending-to-GDP ratios increased by about 2.5 percentage points after the economic shocks in the early 1980s and 1990s, without a strong subsequent decline. Similarly, the global economic crisis that started to unfold in 2007 had a significant effect on the share of economic resources absorbed by welfare states; on average across the OECD, the public social spending-to-GDP ratio increased from around 19 per cent in 2007 to 22 per cent of GDP in 2009 and it has remained at this level since (Figure 5).

During an economic downturn, spending-to-GDP ratios can rise for two reasons: i) because public spending goes up to address the greater need for social support, such as unemployment or housing benefit; and/or ii) GDP grows slowly or declines. Figure 5 disentangles these two effects and shows there was a significant increase in real (adjusted for the GDP deflator) social spending on average across the OECD. In fact, Greece is only one of two OECD countries (the other is Hungary), where real social spending in 2012/13 was lower than in 2007/08; almost half of the OECD countries had lower GDP in 2012/13 than in 2007/08.

The trend of the OECD average masks significant cross-national differences in real GDP growth and real social spending growth since 2007 (Figure 5). Non-European OECD countries had either average real GDP growth or social spending growth, or both – as in Australia (OECD, 2012b). In the United States, at average GDP growth, real social spending growth was above the OECD average, while in Mexico it was real GDP growth rather than social spending trends that substantially differed from the average. In contrast, in Germany real social spending growth was limited compared to most other countries; in the United Kingdom, real spending trends were in line with the OECD average while economic growth was sluggish. In Greece, both real GDP growth and spending growth were well below the OECD average.

Timing varies somewhat across the OECD, but in general, social spending increased markedly during 2007/09 (2008/2010 in the United States), but has stabilized since 2009/2010. Economic growth broadly follows the opposite trend; it
Figure 5. Real public social spending1, real GDP and GDP deflator (Index 100 in 2007, left scale) and public social spending in percentage of GDP (right scale), 2007-13, by level of change between 2007/08 and 2012/13

Change in real public social spending

Below-average (below 8.6%)  Around-average (between 8.6 and 18.8%)  Above-average (above 18.8%)

Notes:
1. Public social spending totals reflect detailed social expenditure programme data for 1980–2009; national aggregates for 2010–2012 and estimates for 2013, as based on national aggregates in national sources, and/or the OECD (2013e), Economic Outlook, No. 93, May 2013, and the EC DG ECFIN (2013) European Union’s Annual Macro-economic database (AMECO), as at May 2013. Spending totals for 2010 to 2012 are subject to revision, but these are likely to be small (light shade); the estimates for 2013 are most likely to be affected by data revisions to spending and GDP (dark shade).

2. Countries are grouped “above”, “average” and “below” in line with the changes to real social spending and real GDP between the average for 2007 and 2008 and the average for 2012 and 2013. The average change in real social spending between 2007–08 and 2012–13 was +13.7% with a standard deviation of 10.1%. The average change in real GDP over the same period was 2.2% with a standard deviation of 9.0% (The OECD average is calculated as the unweighted average for 32 OECD countries (except Japan and Turkey) for which data are available). With around 30 countries in the sample, an observation is statistically significantly different from the average if it is at least half a standard deviation above or below the average change. In case of social spending trends the interval of around average growth from 2007/8 to 2012/13 is 8.6% to 18.8%; for GDP growth from −2.3% to 6.7%.

declined from 2008 to 2009, edged up in 2009/2010 and stabilized thereafter. The initial increase in social spending was in part related to the introduction of one-off payments to pensioners, an easing of eligibility criteria and/or duration of working-age income support programmes as well as family programmes (OECD, 2013d; Richardson, 2011). The increase in the number of benefit recipients was a major contributor to increased spending trends. With the increase in joblessness, spending on unemployment compensation increased from an average of 0.7 per cent of GDP in 2007 across the OECD to 1.1 per cent in 2009. The increase in spending on unemployment benefits from 2008 to 2009 was most pronounced in Iceland from 0.3 per cent of GDP in 2008 to 1.7 per cent in 2009, Ireland from 1.4 per cent to 2.6 per cent, and Spain from 2.2 per cent to 3.5 per cent (OECD, 2012c).

Similarly, in countries where family support is largely income-tested, this contributed to the overall increase in public spending. For example, in the United Kingdom, the rise in the number of low-income families increased both the takeup of such benefits (Child Tax Credit and the Working Tax Credit) and the number of claimants with maximum payments. This contributed to an increase in public spending on family benefits (in-cash, through the tax system, and family services, including childcare) from 3.6 per cent of GDP in 2007 to 4.2 per cent in 2009 (OECD, 2011d; 2013f). The British family payment system did what it was supposed to do, and cushioned the effect of the crisis for poorer families. In 2013, the system will increase its income-tested focus as the hitherto universal child benefit will no longer be paid to the about 1 million households with annual earnings above GBP 60,000.

This early extension of eligibility conditions of working-age income support has been reversed in a number of countries since 2011. For instance in Greece, access to benefits such as unemployment compensation, family benefits, old-age pensions and housing benefits was restricted and/or curtailed in duration, and payment rates for pensions to public-sector workers were cut while other pensions were frozen in nominal terms for the 2011–13 period (OECD, 2012a). Indeed, in Greece, real (as adjusted for GDP deflator) public social spending in 2012/13 was 17 per cent lower than in 2007/08 (and 22 per cent lower than in 2009) and price increases played a significant role in eroding the value of real social spending (Figure 5).

**Concluding remarks**

Conventional measures of public spending are incomplete measures of welfare state effort and they can be improved upon by taking account of private social expenditures which are legally mandated or financially stimulated by government intervention. Furthermore, account should be taken of: tax advantages for social
purposes (e.g. child tax allowances); direct taxation of benefit income; and indirect taxation of consumption by benefit recipients. This leads to greater similarity in total (public and private) social spending levels, particularly when comparing Europe and the United States.

However, similarity in spending levels does not imply similarity of redistribution within welfare systems. In general, the combined effect of spending, targeting and tax burdens and progressivity therein, generates the largest amount of redistribution in welfare systems in Belgium, Finland, Hungary and Slovenia. However, data imperfections restrict the analysis so that the considerable redistributive effects accruing from the general tax-financed provision of social services to children and the elderly in Nordic countries is not captured here (see Förster and Verbist, 2012; Richardson et al., forthcoming). With the crisis, concerns about the acceptability of large income discrepancies have re-emerged: policy-makers have to be concerned about the social sustainability of welfare systems, and for that it is necessary to develop the knowledge base on the redistributive nature of private social benefit arrangements.

Finally, the recent economic crisis had profound effects on social spending trends in most OECD countries. The spending-to-GDP ratios generally increased for two reasons: GDP growth faltered in 2007/09 and the increase in recipients of social benefits and real (adjusted for inflation) social spending reflected the growing need for support. More recently the focus has shifted towards possible benefits cuts, at least in real terms, to curtail public social spending. At the same time as fiscal pressures lead to austerity drives, the demographic outlook is expected to exert upward pressure on social spending trends. Pension system reform is to relieve some pressure on the financial sustainability of pension systems and of social welfare systems more generally in future. Public welfare programmes will be increasingly assessed on their efficiency to provide support to people who need it most, to help people of working-age back to work, and to invest in human capital from an early age onwards.

Bibliography


How much do OECD countries spend on social protection and how redistributive are their tax/benefit systems?


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From pension funds to piggy banks: (Perverse) consequences of the Stability and Growth Pact since the crisis

Bernard H. Casey

Institute for Employment Research, University of Warwick, Coventry, United Kingdom

Abstract As part of their strategy for economic and monetary union, European governments committed themselves to fiscal discipline – particularly by placing limits on annual deficits and on public debt. Subsequently, and as they sought to respond to the “current crisis”, they embraced the view that only if public finances were kept under control would sustainable recovery be possible. Rules of fiscal governance were strengthened. To help them meet these rules, the governments of many member States of the European Union made changes to their pension systems or to funds they had established specifically to pay the costs of population ageing. The intention was not to cut retirement benefits or to improve the efficiency of the relevant pension schemes and institutions. Rather, it was to free up resources immediately. Funded pension

Address for correspondence: Bernard H. Casey, Institute for Employment Research, University of Warwick, Coventry CV4 7AL, United Kingdom; b.casey@warwick.ac.uk.

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schemes and pension funds were treated like “piggy banks” that were raided when times became hard. Moreover, the policies pursued succeeded in meeting their objectives only because the system of national accounts according to which outcomes are judged does not recognize the way in which most of the fiscal gains are matched by future fiscal liabilities.

**Keywords**  pension fund, provident fund, governance, economic crisis, State, European Union

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**Introduction**

A key element of the attempt to achieve economic and monetary union (EMU) was the agreement by the European Union (EU) member States that they would manage public finance in an orderly way. The Maastricht Treaty of 1992 laid out the way in which countries should comply and the procedures for monitoring performance. The most frequently cited of the fiscal requirements was that governments should not run annual deficits in excess of 3 per cent of gross domestic product (GDP) and that total public debt should not exceed 60 per cent of GDP. In the following years, and in order to counter fears that any one member country of the monetary union might “free-ride” upon the others – enjoying the benefits of EMU without implementing the strictures required to ensure its success – the Maastricht provisions were tightened. The Stability and Growth Pact (SGP) of 1996 reinforced the monitoring process that had been specified in the 1992 Treaty and enabled sanctions to be imposed upon governments that ran “excessive deficits”.

Fiscal discipline remained a primary concern of the EU in the years after the common currency was introduced. However, when the fiscal deficit rules were breached by both France and Germany in 2003, neither country was subject to penalty. Rather, the terms of the SGP were relaxed so that greater account was taken of conjuncture and of the intentions for remedy that any country guilty of transgression had committed itself to. It was not until the impact of the crisis that had started in 2008 was being felt, and steps were being taken to mitigate its consequences, that the importance of fiscal discipline was re-asserted. Although some countries had initially responded to the downturn with conventional counter-cyclical measures that included increased expenditure, there very quickly occurred a fundamental reorientation of policy. Fiscal rectitude was given increasing emphasis in almost all the Western countries. Economies, it was argued, could only be stabilized, and growth could only recommence, if public finances were placed in order – in other words, only if a strategy of “expansionary fiscal consolidation” was
pursued. In the EU this led to the adoption of the “six pack” at the end of 2010 – a set of measures that substantially tightened both the preventive and the corrective procedures set out in the SGP. Subsequently, and at the start of 2012, a yet more rigorous Fiscal Compact (the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union) was signed by all but two member States. Under this, governments committed themselves to achieving balanced budgets and debt reduction and to include provisions for the attainment of these ends in their own basic laws. Even the non-signatories of the Compact declared their intent to be bound by its fiscal provisions.

This article is concerned with how meeting the requirements of fiscal discipline had an impact upon pension systems and pension funds in the member States. It is concerned with actions that EU governments took primarily in the interest of meeting conditions set in treaties to which they were a party or achieving targets they had imposed upon themselves – whether keeping public deficit and/or debt within limits, holding down borrowing costs, maintaining the exchange rate of national currency, or generating resources to help meet other political objectives. These actions did not take the form of cuts to retirement benefits. Nor did they take the form of improving the efficiency, and so lowering the costs of operation, of the pension schemes or pension funds in question. Rather, they were directed towards eliminating fiscal costs that were associated with particular types of pension schemes or with taking control of the resources of particular pension funds – in each case, in a way that would help the government in question reduce expenditure, hold down borrowing costs and prevent debt from increasing. Indeed, the implications of the actions taken for the relevant pension schemes as providers of retirement income, or for the pensions funds as sources of wealth out of which future costs of ageing might be paid, were largely incidental and, as will be shown, might not always have been fully thought through. In other words, rather than conducting pension reform or improving the way in which the costs of population ageing might be met, the governments in question effectively treated funded pension schemes and pension funds as “piggy banks”. Like piggy banks, such funded pension schemes and pension funds required feeding and, like piggy banks, they contained wealth. Although their purpose was to provide for future eventualities, like piggy banks, they were vulnerable to raids when unexpected and more immediate needs arose. And it was the crisis that gave rise to such needs.

Many of the relevant actions and measures taken have been reported in the financial media. Some have received attention as part of more general discussions on changes to pension systems that have occurred in recent years (see Casey, 2012; Drahokoupil and Domonkos, 2012; Hirose, 2011; OECD, 2012; Soto, Clements and Eich, 2011). In a few cases, they have been the subject of country case studies (for example, Simonovits, 2011; Milev and Nenovsky, 2012). However, other than
as passing references to them in discussions of policies of “financial repression” (see Reinhart, Kirkegaard and Sbrancia, 2011), there have been few attempts to analyse them from a public finance perspective. Even the European Commission (EC) in its reports concerning actions taken to achieve “stability” or “convergence” or to resolve “excessive deficits” has made only passing reference to them.

For the purposes of making such an analysis it is possible to categorize the measures taken into one of four forms. In a number of cases, they comprised the (temporary) suspension of mandatory funded pension schemes in order to reduce “transition costs”. In some cases, they comprised the sequestration of funds that had been built up to meet members’ accumulated retirement benefits. In other cases, they comprised governments prematurely tapping the resources of pension reserve funds that had been set up to meet future costs of ageing. Last, in some cases, they comprised governments influencing or seeking to influence the investment behaviour of funds in a way that would be beneficial to public finance. These four forms of action are described in the following four sections of this article. A final section draws conclusions.

Saving money by cutting transition costs

Pension reforms that generated transition costs were made in many of the “new” (or post-2004) member States of Central and Eastern Europe (CEE). Most of these countries sought to refashion the systems they had inherited from the “socialist” past to make them more appropriate to the “market” economies they aspired to become. One of the ways many adopted was to introduce a funded component to their pension system. This involved the introduction of mandatory individual accounts into which a share of contribution income was diverted. The switch to private funding would, eventually, reduce the outgoings of the public social security system, but in the short- and medium-term the latter system was deprived of some of its income whilst its expenditure – payments to people who had built up rights under the old provision – remained unchanged. All other things being equal, making up the shortfall required additional income and/or additional borrowing. Savings might be generated by other reforms to the pension system, but these savings would have been available for other uses and so would not diminish the effective cost of transition. In fact, it was not only CEE countries that made changes to their pension schemes that generated such costs. A component of the Swedish pension reform that took effect in 2000 consisted of allocating a proportion of contributions to the public pillar pension scheme into a funded, individual account – the PPM (Sundén, 2001).

The size of the diversion from the first pillar, and so the size of the transition cost, varied between countries. Amongst those countries where a substantial amount of contributions was switched were Slovakia, where some 9 per cent of...
earnings went to the newly-established second pillar, Latvia and Hungary, where the relevant figure was 8 per cent, and Poland, where it was over 7 per cent. More modest were the diversions in Lithuania (5.5 per cent of earnings) and Estonia (4 per cent of earnings). The smallest diversion was in Sweden with 2.5 per cent of earnings.

In the reforming countries, it was generally understood that transition costs would, eventually, arise. Projections of the size of the deficit that would ensue, and of the time over which it would extend, were often too optimistic. The EC noted how “in some member States, however, the net transition costs turned out to be higher than anticipated” (EC, 2010, p. 58), whilst the International Monetary Fund (IMF) described in more detail the specific case of Poland where initial assumptions about economic growth and labour force participation were too high, whilst those about the number of people who would chose to switch to the funded system were too low (Epstein and Velculescu, 2011, pp. 12–13).

Under “normal” circumstances, transition costs might have been tolerable, and reforming governments might have expected forbearance to be shown. Initially, this appeared to be the case. Indeed, when in the more benign times of the early-to mid-2000s the SGP was revised to cope with the breaches to the deficit rule that were being made by France and Germany, pension-reforming countries sought and achieved a quid pro quo. The revised treaty included the provision that, from 2005, countries making pension reforms that included the introduction of a mandatory, fully-funded pillar could request that the costs of such reform be taken into account if their deficits exceeded the 3 per cent reference level. The caveat was that the deficit, if above 3 per cent, had to be “close” to it, that account would be taken of the extent to which any excessive deficits had been corrected, and that, in any case, the amount of extra costs taken into account would fall gradually to zero over the following five years (ECB, 2005).

Estimates of the size of the impact of pension reform on the fiscal deficit have been made for a number of CEE countries (Table 1). At least one estimate has also been made for Sweden. In 2007, only two countries were running deficits in excess of 3 per cent of GDP. However, in four countries transition costs were equal to, or in excess of, 1 per cent of GDP.

By the end of the decade, when the relief granted by the 2005 reform of the SGP was due to expire, the reforming countries sought an extension of its terms. However, by this time the economic and political environment was very different. Three of the reforming countries had been sufficiently badly hit by the crisis that they had already been forced to seek assistance from the IMF – Latvia and Hungary in 2008, and Romania in 2009. This assistance was made conditional upon their governments adopting policies of fiscal retrenchment. Seven – all but Estonia and Sweden – were running deficits in excess of 3 per cent, and demands for fiscal rectitude were being intensified. The new code of conduct on
the operation of the SGP both tightened excessive deficit procedures further and limited any forbearance of transition cost to countries where “as long as the general government deficit does not significantly exceed a level that can be considered close to the 3 per cent of GDP reference value and the debt ratio does not exceed the 60 per cent of GDP reference value, on condition that overall fiscal sustainability is maintained” (EC, 2012b, p. 10).

With other revenues declining, a number of CEE governments took steps to reduce, at least temporarily, some part of the payments into individual accounts and to use contribution income to help meet current expenditure needs (Table 2). The government of Lithuania was the first to make such a move, but others rapidly followed suit.

Suspension of contributions to funded pension schemes was not, in fact, a peculiarly Eastern European phenomenon. Two German states – Thuringia and Bavaria – stopped paying contributions into funds that were intended to finance the pensions of their civil servants. In each case, the state government cited the financial crisis, and consequent pressures on public expenditure, as the reason for their doing so (Ottawa, 2011).

**Sequestration of private pension funds**

Merely suspending contributions to the second pillar funds proved inadequate for the government of Hungary. In 2011, all contributors to second pillar funds, unless

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**Table 1. Impact of pension reform on fiscal situation in 2007 (percentage of GDP)**

<table>
<thead>
<tr>
<th>Country</th>
<th>Fiscal balance as recorded (1)</th>
<th>Transition cost (2)</th>
<th>Fiscal balance if no reform (3) = (1)–(2)</th>
<th>Fiscal balance as recorded in 2009 (4)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bulgaria</td>
<td>0.1</td>
<td>−0.7</td>
<td>0.8</td>
<td>−4.3</td>
</tr>
<tr>
<td>Estonia</td>
<td>2.6</td>
<td>−1.3</td>
<td>3.9</td>
<td>−2.0</td>
</tr>
<tr>
<td>Latvia</td>
<td>−0.3</td>
<td>−0.8</td>
<td>0.5</td>
<td>−9.8</td>
</tr>
<tr>
<td>Lithuania</td>
<td>−1.0</td>
<td>−0.9</td>
<td>−0.1</td>
<td>−9.4</td>
</tr>
<tr>
<td>Hungary</td>
<td>−5.0</td>
<td>−1.2</td>
<td>−3.8</td>
<td>−4.6**</td>
</tr>
<tr>
<td>Poland</td>
<td>−1.9</td>
<td>−1.3</td>
<td>−0.6</td>
<td>−7.4</td>
</tr>
<tr>
<td>Romania*</td>
<td>−5.4</td>
<td>−0.3</td>
<td>−5.1</td>
<td>−9.0</td>
</tr>
<tr>
<td>Slovakia</td>
<td>−1.9</td>
<td>−1.0</td>
<td>−0.9</td>
<td>−8.0</td>
</tr>
<tr>
<td>Sweden</td>
<td>3.6</td>
<td>−0.8</td>
<td>4.5</td>
<td>−0.7</td>
</tr>
</tbody>
</table>

* Romania, 2008, the year the reform was made.
** Government debt was also in excess of 60 per cent of GDP (79.8 per cent).

they specifically chose otherwise, were switched back into the public pension scheme. Those who did not were told they would earn no further accruals under the latter. Shortly afterwards, it was announced that the assets of the pension funds – worth well over 10 per cent of GDP – were to be transferred to the government account. The monies were to be used to reduce government debt, to finance current expenditure, or, it has been suggested, to pay for the move to a (lower) flat-rate income tax. Future pensioners would be treated as if they had never left the first pillar, although they also received any positive real yields that had been earned on their second pillar accounts (Simonovits, 2011).

The Hungarian government was not the first to view pension scheme assets as a source of relief for fiscal shortfalls. Already in 2008, but before the world financial crisis had hit the country, the government of Argentina had nationalized the accounts of the supplementary pension funds (Kay, 2009). Nor was Hungary alone in Europe (Table 3). At an early stage of Ireland’s experience of the crisis, its government took a similar step, albeit on a more limited scale. The pension fund of the public universities and certain other public agencies was transferred to the Irish Exchequer in return for an agreement to meet future payments out of current expenditure (Stewart, 2009a and b). Equally, in late 2010, the government of

Table 2. (Temporary) actions taken to reduce transition costs (contributions as percentage of covered wages)

<table>
<thead>
<tr>
<th>Country and year initiated</th>
<th>Total pension contribution</th>
<th>Diverted to individual account</th>
<th>Diverted after reform</th>
<th>Reversion date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Estonia 2009</td>
<td>20.0</td>
<td>4.0*</td>
<td>0.0</td>
<td>Back to 2.0 in 2011 and to 4.0 in 2012; raised to 6.0 2014–17 for those who continued own contribution during suspension*</td>
</tr>
<tr>
<td>Latvia 2009</td>
<td>20.0</td>
<td>8.0**</td>
<td>2.0</td>
<td>Latest proposal, back to 4.0 in 2014 and 6.0 in 2015 or 2016</td>
</tr>
<tr>
<td>Lithuania 2009</td>
<td>18.5</td>
<td>5.5</td>
<td>2.0</td>
<td>Reduced to 1.5 in 2012, increased to 2.5 in 2013, back to 2.0 in 2014, but those contributing an additional 1% receive a further 1% of national average wage as contribution from government</td>
</tr>
<tr>
<td>Romania 2009</td>
<td>19.5</td>
<td>2.0 and rising 0.5 p.a. to 6</td>
<td>Frozen at 2.0 in 2009</td>
<td>0.5 increases restarted in 2010, to reach 6.0 by 2017</td>
</tr>
<tr>
<td>Poland 2011</td>
<td>19.5</td>
<td>7.3</td>
<td>2.3</td>
<td>Gradually rising to 3.5 by 2017</td>
</tr>
<tr>
<td>Hungary 2011</td>
<td>31.0</td>
<td>8.0</td>
<td>Initially to zero</td>
<td>Subsequently, scheme nationalized</td>
</tr>
<tr>
<td>Slovakia 2012</td>
<td>18.0</td>
<td>9.0</td>
<td>4.0</td>
<td></td>
</tr>
</tbody>
</table>

* Plus additional 2 per cent from employee also diverted to social security. 
** Was due to rise to 10 per cent in 2010.
Portugal, which had already had to apply for a Eurozone “bailout”, took over the assets of the pension fund of the national telecom company and, subsequently, the pension fund of the banks – worth, respectively, 1.5 and 3.5 per cent of GDP. According to contemporary reports, part of the proceeds of the initial action was used to pay for two submarines that the defence ministry had purchased (Williams, 2010a and b; Sourbes, 2011).

Although not presented as a sequestration, the actions of the United Kingdom government with respect to the pension scheme of the state-owned mail delivery service had a beneficial fiscal side effect. There had been a long-standing desire to privatize the mail service – in part to meet EU competition regulations, in part to attract the capital necessary for modernization and to reduce losses borne by the Exchequer. However, attempts to realize this objective had foundered, not only because of political opposition but also because of the underfunded – in the order of 25 per cent – pension obligations any buyer would have had to take on. To smooth the way for a sale, the government agreed to take over the responsibility for paying pensions and in return took control of pension fund assets worth nearly 2 per cent of GDP (Groom, 2012; IFS, 2012).

Also not presented as a sequestration was the way in which, under the Eurozone rescue package for Cyprus that was agreed in early 2013, pension and provident funds were obliged to participate in the recapitalization of the country’s banking system. Already at the end of 2012, the Cyprus government had found itself sufficiently close to default that it had approached a series of semi-government organizations – the Telecommunications Authority, the Electricity Authority and the Cyprus Ports Authority – for temporary loans. All three acceded to the request – thereby, it was said, enabling the government to meet its end-of-year salary commitments. Whilst the Port Authority drew from its reserves, the other two organizations allocated assets from their pension funds. When a rescue plan was

<table>
<thead>
<tr>
<th>Country</th>
<th>Pension Fund</th>
<th>Size as percentage of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Portugal</td>
<td>Telecom</td>
<td>1.3</td>
</tr>
<tr>
<td></td>
<td>Banks</td>
<td>4.6</td>
</tr>
<tr>
<td>Ireland</td>
<td>Universities, etc.</td>
<td>1.1</td>
</tr>
<tr>
<td>Hungary</td>
<td>Second pillar</td>
<td>10.7</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>Royal Mail</td>
<td>1.8</td>
</tr>
<tr>
<td>Cyprus</td>
<td>Pension and provident funds</td>
<td>approx. 20.0</td>
</tr>
</tbody>
</table>

Source: Own calculations from sources cited in text; own estimates.

Table 3. Size of pension funds sequestered or nationalized (as percentage of GDP, year before intervention).
finally concluded, it involved the bailing-in of “uninsured depositors” at the two large banks that had failed. The “uninsured deposits” included a substantial part of the assets of the country’s pension and provident funds. The latter, unlike their counterparts in many countries, had invested much of their assets not in equities or (government) bonds but in interest bearing bank deposits. Almost without exception, the size of their balances exceeded the EUR 100,000 threshold that was protected in the event of bank insolvency. A “haircut” of 47.5 per cent was applied to these. A plan that would protect the provident funds – which operate on a defined contribution basis – by ensuring that they did not suffer losses in excess of 25 per cent has been offered by the government, but it will not be applied to pension funds – which operate on a defined benefit basis – leaving the sponsors of the schemes to make up any losses that ensue (Casey and Yiallouros, 2013).

**Prematurely accessing pension reserve funds**

National pension reserve funds fall into two types – social security reserve funds and sovereign pension reserve funds. The former draw their income from social security contribution income (even if this includes contributions made by government as a “third payer”), whilst the latter stand outside social security systems and rely largely on direct fiscal transfers from the government. Both types of funds are intended to smooth income and expenditure, although sovereign reserve funds tend to be more specific with respect to when they can be drawn upon – often by setting a specific date before which assets cannot be touched (Blundell-Wignall, Hu and Yermo, 2008). Empirically, there is no difference between the two types of fund in terms of size, but both are larger than the “buffer funds” that most social security authorities have for the purposes of managing short-term fluctuations in income or expenditure.

Reserve funds are investors. They can be given mandates with respect to their investment behaviour, and how they invest can have implications for the economy of the country in which they operate. Some funds are merely required to maximize returns, others are set social objectives. However, once objectives have been set, it is considered desirable that sponsoring governments maintain a hands-off stance (Yermo, 2008).

As the impact of the crisis intensified, a number of European governments intervened in the operation of reserve funds to help meet their fiscal targets. These interventions took two forms. In some cases, governments drew down on a fund’s resources. This was the case in France, in Poland and in Spain (Table 4). The 2010 “Fillon Reform” of the French public pension scheme is best remembered for its raising of the pension age above 60. Less remarked upon was that it also involved the government changing the task of the Pension Reserve Fund (Fonds de Réserve pour les Retraites, FRR). This fund had been established in 1999 to help finance
shortfalls in contribution income that were foreseen in the future. It has been provisioned by (temporary) surpluses in selected social security funds, additional taxes on private assets, and the proceeds of privatizations and of auctions of telecommunication licences, as well as any returns on the investments it has made. The fund was not intended to start making disbursements until 2020. However, this was changed in 2010. Disbursements started in 2011 with payments going to meet deficits currently already arising or projected in the social security system. Rather than being exhausted only in 2042, the fund will now be exhausted in 2024. The short-term benefit to public finances was not inconsiderable. In the National Reform Programme 2011–2014 that it submitted to the EC under the terms of the Maastricht process, the French government described the pension reform it had undertaken as reducing government debt in 2020 by 10 percentage points, of which 2 percentage points came from the early utilization of the reserve fund (Government of France, 2011, p. 15).

Poland had set up a Demographic Reserve Fund (Fundusz Rezerwy Demograficznej, FRD) in 1998 that would receive both revenue from the social security system and a share of receipts from privatizations. By 2010, the fund had accumulated resources worth some 2 per cent of GDP. However, in that year, in order to help the country satisfy the Maastricht requirements, and to assist it in meeting a self-imposed (constitutional) requirement to keep gross debt below 55 per cent of GDP, the government dug into the FRD. A second sequestration occurred in the following year, with the two withdrawals together reducing the size of the fund by some 50 per cent.

In Spain, a Social Security Reserve Fund (Fondo de Reserva de la Seguridad Social, FRSS) rather than a sovereign pension reserve fund was put in place. It started operating in 2000. Its income came from surpluses run by the operation of the social security system and a decade later the fund was worth over 5 per cent of GDP. Spain was one of the countries hit particularly hard by the crisis, which not only led to massive increases in unemployment and a fall in tax revenues but also exposed deficits and debts in the balance sheets of regional administrations and

Table 4. **Size of “reserve” funds prematurely accessed (as percentage of GDP, year before intervention)**

<table>
<thead>
<tr>
<th>Country</th>
<th>Reserve Fund</th>
<th>Size as percentage of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>France</td>
<td>Pension Reserve Fund</td>
<td>2</td>
</tr>
<tr>
<td>Spain</td>
<td>Social Security Reserve Fund</td>
<td>6</td>
</tr>
<tr>
<td>Poland</td>
<td>Demographic Reserve Fund</td>
<td>2</td>
</tr>
</tbody>
</table>

Source: National reports of the funds and own calculations.
required the bailing-out of banks. The country’s fiscal balance went from being in surplus of 2 per cent to deficit of over 11 per cent in 2009 and it was still near to 11 per cent in 2012. The resources of the fund were drawn upon twice in late 2012 to help fill gaps in the central government’s account, and a third time in mid-2013 explicitly to meet pension payments (Fixsen, 2013). The sums involved were relatively small – together constituting little over 16 per cent of the total that had been built up.

Influencing fund investment behaviour

The second way in which governments were able to make use of pension reserve funds (and other pension funds) was to influence the way in which their assets were invested. The Spanish FRSS was permitted to hold only government paper and only that from Spain, France, Germany and the Netherlands. Within these limits, its portfolio was fairly diversified – although the share of domestic bonds held grew over time. A dramatic change came after 2008. In that year, domestic bonds made up some 54 per cent of the portfolio, in the following year they made up nearly 77 per cent and, by 2012, over 97 per cent. Whether or not it was declared as such, selling off foreign bonds and the purchasing of domestic bonds fitted a strategy of trying to push up the price of the latter and thus to stem the rise in the rate of interest that purchasers in Spanish debt were demanding. It was certainly consistent with the government’s efforts to avoid having to request bailout assistance from its Eurozone partners.

The use of a sovereign pension reserve fund to mitigate the impact of the crisis on a country’s public finances that has attracted most notice has been that which occurred in Ireland. Ireland, which was recognized as benefiting from a “demographic dividend”, had set up a National Pensions Reserve Fund (NPRF) in 2001. The government committed payments of 1 per cent of GDP into the fund each year, and the intention was to start drawing resources down in 2025. Assets were invested to maximize returns under the oversight of an independent commission, and already by 2007 the NPRF was worth over 13 per cent of GDP. However, faced with the need to recapitalize the banking sector, in 2009 the government altered the fund’s mandate and “directed” it to invest in newly-issued preference shares in two major banks. These purchases were to be financed by the selling-off of other assets, the liquidation of cash reserves and by an additional allocation to the NPRF from the Irish Exchequer. This allocation supplemented the one that had already occurred when the fund became the recipient of the sequestered resources of the universities’ and other pension funds (NPRF, 2010).

The initial efforts to rescue the banking sector proved inadequate, and in late 2010 the Irish government applied for assistance under Eurozone rescue procedures. The settlement that was reached included the government agreeing to
commit a further tranche of national resources to bank recapitalization, and a
large share of these – EUR 10 billion of the EUR 17.5 billion in question – was
provided by the NPRF. The result was that by the end of 2011, some 60 per cent of
the fund’s assets were in what since 2009 had been designated its “directed portfo-
ilio”. Although the remaining investments, which were held in what was now
 termed the “discretionary portfolio”, performed relatively well and recorded an
increase in their value over the years 2010 and 2011, those in the “directed portfo-
ilio” recorded substantial losses as the bank share prices fell (Table 5). The net result
was that the fund as a whole was losing money. Equally important, whilst the assets
of the discretionary portfolio continued to be counted as an offset to public debt,
those of the directed portfolio did not.

In the end, not even the discretionary portfolio was left alone. In 2011 the gov-
ernment announced an initiative whereby resources from the NPRF would be
channelled towards productive investment in sectors of strategic importance to the
Irish economy (NPRF, 2012). Here reference was made to the small and medium-
sized enterprise sector, the high-technology sector and infrastructure. Such invest-
ments were to be made on a commercial basis, and would involve private-sector
partners investing their own resources. The first investment decisions were made
in late 2012 and early 2013. By consenting to participate in the initiative, the fund
completed its transformation from being an institution that assisted the country in
meeting the cost of societal ageing to one that assisted it in restoring economic sta-


tility and engendering growth. The *de facto* transformation became *a de jure* one
when, in mid-2013, the government announced plans to abolish the NPRF entirely
and to hand the assets that remained in its discretionary portfolio to a new Ireland
Strategic Investment Fund (ISIF) under the control of the Ministry of Finance and
its National Treasury Management Agency and dedicated to making investments in
the domestic economy. Moreover, although resources would continue to be allo-
cated to the ISIF at the same level as they had previously been to the NPRF, the
objective of pre-funding the cost of societal ageing was formally abandoned. The

### Table 5. Returns on Irish NPRF and constituent portfolios (percentage), 2008–2012

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discretionary</td>
<td>NA</td>
<td>20.6</td>
<td>11.7</td>
<td>2.1</td>
<td>7.3</td>
</tr>
<tr>
<td>Directed</td>
<td>NA</td>
<td>0</td>
<td>−25.7</td>
<td>−58.1</td>
<td>10.4</td>
</tr>
<tr>
<td>Total</td>
<td>−30.4</td>
<td>11.5</td>
<td>−3.0</td>
<td>−36.7</td>
<td>9.1</td>
</tr>
<tr>
<td>Directed as percentage of total at end of year</td>
<td>NA</td>
<td>31.0</td>
<td>33.6</td>
<td>59.7</td>
<td>58.5</td>
</tr>
</tbody>
</table>

*Note: NA = not applicable.*

*Source: NPRF annual and quarterly reports.*
government argued that, “[w]hile the need for the state to provide for social welfare and public service pensions obligations has not abated, fostering economic activity and employment is currently a greater priority” (Department of Finance, 2013) (see Box 1).

Last, it is worth noting that the United Kingdom and the Dutch governments have also seen that assets of occupational pension funds might be turned to serving macro-economic objectives. The British government acknowledged that projects to develop the country’s physical infrastructure could give an impetus to economic growth and have an immediate employment effect. However, it was not prepared to make the expenditures required itself, because this would increase public spending. Instead, it encouraged pension funds, and particularly those of local governments (the central government scheme is “unfunded”), to allocate a greater share of their assets to activities that would serve such a purpose, and it

Box 1. Fiscal repression: Obligating investment in infrastructure

A further dimension of the re-reform of the Polish pension system has been a call by the Ministry of Administration and Digitization for the second-tier pension funds (OFEs) to play a greater role in infrastructure investment – in particular, in the roll-out of local high-speed broadband. Poland already has an embryonic Infrastructure Fund (Polskie Inwestycje Rozwojowe – PIR). Initially, it was envisaged the Fund would use earnings from the privatization of state companies to finance a range of investments, including in energy roadways. However, with most publically-owned assets already sold off, alternative sources of finance are being sought.

Meanwhile, the government of Croatia has indicated that it might not proceed with plans to increase the share of contributions that goes into the mandatory second pillar unless pension funds invest more in capital and infrastructure. The Croatian system has maintained a five percentage point diversion of contributions into private funds since its inception in 2002 (the total contribution rate is 20 per cent) and, unlike many other CEE countries, the government made no (temporary) changes in the years following the crisis. However, at the start of 2014, Croatia, which had joined the EU only six months previously, was placed under “excessive deficit procedures” – a budget shortfall of 6.4 per cent had been projected. The government’s proposal not to switch more contributions to the second pillar has been seen as jeopardizing plans for (some) pension funds to acquire assets in the main state-owned toll road. The current toll-road authority is reported to have debts worth some seven per cent of GDP and some share of these would pass from the state’s books to those of the pension funds if the privatization went ahead.
proposed ways in which the risks that deter them from such behaviour might be mitigated (Rowley, 2011). The government’s initiative received a broadly favourable response from the pension funds and the organizations representing them, and led to the latter establishing a Pension Infrastructure Platform. On the other hand, the amount of investment this aims to generate represents at best one tenth of the GBP 20 billion of spending that the government hoped to achieve.

The task foreseen for domestic pension funds by the Dutch government is that of helping to bolster the residential housing market where prices have fallen by a fifth since 2008 and where a quarter of property owners are currently in negative equity. Its proposition is for banks to sell mortgage-backed bonds guaranteed in the last instance by the State, thereby both improving the balance sheets of the issuers and increasing their ability to lend to house buyers. Pension funds have tended to be sceptical; so, too, has been the IMF (Preesman, 2013; IMF, 2013). The former have stressed that they “are not a philanthropic institution” and that their “task is to offer purchasing power for the participants of [their] clients”, whilst the latter has repeated macro-prudential concerns about the persistence of a housing price bubble.

**Conclusions**

It is claimed that on being asked by the trial judge why he robbed banks, the accused, Willy Sutton, answered “because that is where the money is” (Sutton, 1976). Analogously, it might be suggested that fiscally-challenged governments took to backtracking on pension reforms and exploiting the resources of pension funds because such actions provided easy access to additional income. What is more, the actions and initiatives described in this article went largely unchallenged.

It was probably the financial services industry, and particularly asset managers and insurance companies that earned income from their role in administering and investing the assets of second pillar pension funds and pension reserve funds, which adopted the most critical stance. The smaller the flow of contributions into such funds was, the less business for them there was, and the less viable that business became. In the case of nationalization, as occurred in Hungary, a whole line of insurance activity was closed down (Escritt, 2012; Ottawa, 2012a and b). Concerns that the Hungarian policy might be repeated were expressed by pension industry representatives in both Bulgaria – in late 2012 – and Poland – throughout the first half of 2013 (Krzyzak, 2013c). In the first of these two countries, the government was under political pressure to increase spending in order to alleviate some of the hardship caused by economic downturn and the austerity measures it had taken to reduce an excessive fiscal deficit (Ottawa, 2012c). In the second, the fact that the government was obliged to reduce an “excessive deficit” fuelled suspicions that the resources of the second pillar funds might be used to help improve the fiscal
balance and to keep debt below the limit set by the constitution. In the case of Bulgaria, fears have not (as yet) been realized. In Poland, by contrast, the government has proceeded with legislation to hold the contribution rate to the second pillar funds at just under 3 per cent, require those choosing to stay in it to contribute an additional 2 per cent of salary, and prevent the funds from investing in domestic government bonds. The same legislation also allows the government to take over (and retire) the funds’ entire existing domestic bond holdings. This last would lead to a once-off reduction of government debt by 8 percentage points of GDP (Krzyzak, 2013a and e). That such proposals not only continue to be made but also to be put into effect indicates that pension funds remain low hanging fruit that is ripe for picking. The closure of the Irish National Pension Reserve Fund announced in mid-2013 showed that, in extremis, little is sacred.

The sequestration of pension assets might be considered a violation of property rights, and arguments concerning this were raised when the Polish government persisted with its 2013 reform proposals (Krzyzak, 2013d). However, the extent to which pension fund contributors were conscious of this change when their contributions stayed the same but were merely directed to another recipient is difficult to judge. Participation in funded second pillars, where it had been voluntary, had proved higher than anticipated – one of the reasons why many of the initial projections of transition costs had been over-optimistic. Nevertheless, in many countries, there has also been criticism about the charges that funds are levying and upon the performance of the investments they have been making. Fund members might not have been as aware of how well or badly they were being served as were the specialists who analysed the schemes’ performance for the purposes of appraising the merits and demerits of pension reforms. However, at the same time that fears for the future of the second pillar were being expressed in Bulgaria, the government was quoted as describing current arrangements as “badly managed” (Ottawa, 2012c). Equally, when proposals for the closure of the second pillar in Poland and the transfer of its assets back to the first pillar were first discussed, concerns about the level of charges were also being expressed (Krzyzak, 2013b). Moreover, the Hungarian government made reference to shortcomings with respect both to charges and to investment performance when justifying its abolition of the second pillar (Escrítt, 2012; Simonovits, 2011). Whether Hungarian savers were thankful for what was done is less clear. There have been suggestions that the government’s action diminished trust in domestic financial institutions and even precipitated efforts by holders of bank accounts to move funds abroad for fear that the assets they held there might also be taken (Eddy, 2012). The same might be said with respect to Cyprus. There are indications that the members of some provident funds, being so disenchanted by the cut in the value of the pay-out that these will make, have been successful in demanding their dissolution (Casey and Yiallouros, 2013).
The extent to which actions taken with respect to reserve funds attracted attention is likely to have been influenced both by the prominence of the intervention and by the size of the fund. When the French government announced its proposals to access the FRR earlier than initially envisaged, it provoked the critical response that resources which had been allocated to help finance the old age of the baby boomers were now being used to finance the old age of the “papy boomers” (Bridier, 2010). On top of this came arguments that the move was symptomatic of too great a reliance being placed on a pay-as-you-go rather than a funded scheme – the reserve fund being one of the ways in which a diversification of financing was being supported (Amenc et al., 2010). Within any one reserve fund, an increasing concentration on domestic investments runs counter to the principle of diversification. The Irish NPRF, before the government started directing its investments, had had almost none of its investments in its home country, and that had been part of a deliberate strategy. Moreover, it might be asked how prudent it was for the Spanish FRSS to have increased exposure to domestic government bonds. The price of these did, initially, rise, but it has been volatile and has fallen as confidence in the government’s ability to manage a way out of the crisis evaporates. Equally, the logic of using pension fund resources to finance infrastructure can also be questioned. Certainly, with respect to the United Kingdom, it could be argued that pension funds would require a higher return on their investment than the government would have to pay were it to borrow outright. In addition, had the government borrowed outright, it could have issued the sort of long-term bonds for which pension funds are said to be hungry. The depletion of the Polish FRD provoked repeated criticism from the Monetary Policy Council of the country’s national bank, which saw the use of its resources to pay for the ongoing service of old-age pension benefits as not supporting the long-term sustainability of public finance (NBP, 2010). Similarly, the head of the Spanish FRSS conceded that tapping into the reserve fund for extraordinary payments could lead to “some problems” in the future if the country’s economy does not improve (Fixsen, 2013). In contrast, responses to the transformation of the Irish NPRF have been somewhat ambiguous. From its inception, there had been some who had asked why resources had been paid into the fund at the same time that public investment needs were unmet (Slattery, 2010). Once the crisis hit Ireland with its full force, there were those who pointed out it was cheaper for the government to borrow from the NPRF than from other, external sources (Moriaty, 2012). Nonetheless, the changes the government made to its remit meant that it took on the role first of supporting the banking system and then of modernizing the entire economy. Whether the fund will ever be able to recoup the losses incurred on its directed portfolio is highly questionable. Yet, if bank recapitalization was a necessary condition for recovery to ensue, ensuring it was achieved would enhance Ireland’s ability to make acceptable
provision for an ageing society in the years after 2025. Equally, the government justified the transformation of the fund into a provider of infrastructure finance with the argument that using its resources for this purpose would “put the state in a better position to meet its pensions’ obligations in the longer term” (Williams, 2013).

Of greatest interest, however, are the responses to the actions and initiatives described in this article from those who were monitoring fiscal conduct. The governments of the member States file stability or convergence reports on an annual or biannual basis with the EC, which comments upon them and uses them to prepare the recommendations issues by the European Council. It was a fear of the strictures and criticisms that might be levelled at them which had prompted countries that had undertaken pension reforms generating transition costs to press for an extension of forbearance when their fiscal deficits were being appraised. The response that they received suggested that they should, instead, pursue even stricter austerity programmes. However, when the Commission came to comment on the switching of contributions back to the first pillar of the pension system, it was remarkably uncritical. Its response to the Latvian government’s convergence report is worthy of citation. Referring to the 6 percentage point reallocation of contributions to pillar one – one of the more substantial re-diversifications and one for which, at that time, plans for any reversal remained rather vague – it described it as “a temporary measure [that can be] excluded from the structural balance. Thus, its reversal in 2013 will affect only the nominal but not the structural balance” (EC, 2012a, p. 9). Indeed, in mid-2012 both the Commission and the European Central Bank were able to report that the country was satisfying convergence criteria and would be permitted to join the common currency at the start of 2014. Estonia, another country that had temporarily suspended contributions to the second pillar to improve its fiscal deficit, was deemed fit for membership in 2010. Lithuania, which was able to take advantage of the SGP provision that allowed transition costs to be offset, exited its excess deficit procedure in early 2013 and followed this up with a request for approval of its application to join the common currency to be speeded up.

When making its first review of Portugal’s progress under the terms of the Eurozone bailout, the Commission referred to the pension fund sequestrations that its government had made, but it described these as contributing to short-term stabilization and did not censure them (EC, 2011a). Yet more noteworthy, however, was the response of the Commission when, together with the European Central Bank (ECB) and the IMF, it was constructing a rescue package for Ireland. In this case, it formally approved the recasting of the role of the NPRF, as an integral part of the programme it was signing off. Only the nationalization of the second pillar funds in Hungary appeared to provoke concern. Here, the Commission concluded that although this “account[ed] for a large part of the sharp debt reduction in
2011, [it] significantly increase[d] the long-term implicit liabilities of the budget” (EC, 2011b, p. 10).

What is noteworthy in the last of these judgements is the term “implicit”. The actions and initiatives were undertaken because they brought about short-term fiscal relief. Although they were seen as being no more than palliative, they were not, per se, condemned. The targets set by the Maastricht process as it was initially established, and even those that were subsequently imposed, were all concerned with the short-term. Even the medium-term objectives that governments are supposed to fulfil refer only to the next five years. Moreover, the targets were for explicit deficits – more specifically, explicit structural deficits – and explicit debt. Despite the fact that the Commission, via its Ageing Working Group, has produced projections of pension expenditure until well in the future, it has not sought to convert the stream of expenditures into current debt and thereby to make it explicit. Yet more important, although some individual governments have reported their estimates of implicit debts when making up their own national accounts, the European System of National Accounts, which they have to apply when reporting their fiscal position, do not record such debt (European Parliament, 2011; see also Lojsch, Rodríguez-Vives and Slavík, 2011). Accordingly, any re-diversion of contributions to the first pillar pension is counted as a revenue gain, whilst any future first pillar pension entitlements that are built up as a consequence are not recognized as additional expenditures that have to be offset against it. The same applies when pension funds are sequestered or nationalized. Such actions can produce substantial income in the year that they occur – income that, in that year, far exceeds the costs of the pensions that will have to be paid in the future if contractual entitlements are respected.

Prematurely accessing pension reserve funds does have an impact upon a government’s fiscal balance in so far as a reduction in the value of assets held is the equivalent of an increase in government debt. The smallness of the sums involved relative to total debt of the countries concerned might explain why the premature access of such funds has incurred scarcely any mention when the fiscal stance of these countries has been evaluated. So, too, might be the fact that the Maastricht debt targets have never been enforced with the same rigour as the deficit targets. What is more, in the case of Ireland, the increase in debt that resulted from the reclassification of a substantial share of the reserve fund’s assets was an integral part of the rescue package that the EC, the ECB and the IMF had helped draw up and to which they gave their formal approval.

In short, there were few restraints upon governments using pension funds as piggy banks. Indeed, that they could do so was one of the perverse consequences of the Stability and Growth Pact. What is much less clear is what the wider costs and benefits of their actions were. Making judgements about these requires making projections of the retirement benefits that contributors might expect.
under pension schemes before and after the latest round of reform, re-reform or un-reform. The outcome of such exercises is often highly sensitive to the assumptions on which they are based. It also requires making judgements about whether using resources now to cope with current challenges is more productive than setting these resources aside to cope with projected future challenges. The decisions that are made in such cases are usually based upon the weight policy-makers give to the interests of today’s generations relative to those of tomorrow’s generations and this, implicitly, determines the discount rate that is used. More important than this, however, making judgements about the wider costs and benefits of the actions described in this article requires an evaluation of the appropriateness and efficacy of the overall macro-economic strategy that European governments are pursuing. All this, however, is beyond the scope of this article, which merely aims to show what happened once governments had adopted such a strategy requiring them to concentrate attention on reducing fiscal deficits and debts. When this became the objective, and when it was headline deficits and debt to which most attention was paid, it was hardly surprising that they were tempted to use pension funds as piggy banks.

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From pension funds to piggy banks


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From pension funds to piggy banks


Extending social security coverage to the rural sector in China

Tianhong Chen and John A. Turner

Wuhan University, Wuhan, China; Pension Policy Center, Washington, United States

Abstract  In late 2009 China launched an innovative, voluntary programme that by 2011 had extended pension coverage to 326.4 million people in the rural sector, including contributors and beneficiaries. It requires one contribution per year and provides a flat-rate benefit and a contributions-related benefit through a contributory individual account, with a government guarantee that the benefit will continue for life. The programme encourages participation of persons who do not pay income taxes, and thus have no tax incentive to participate, by providing substantial government subsidies. As a further incentive, old-age benefits are provided to older parents when all their adult children participate in the contributory programme.

Keywords  old age benefit, gaps in coverage, pension scheme, social security financing, China

Introduction

China is undergoing a period of important changes in its provision of old-age benefits. At the start of 2009, less than 30 per cent of its adult population was covered by a social security old-age benefits programme, but in 2012 that figure had increased to 55 per cent (The Economist, 2012).
Like in many countries, until recently people living in rural areas in China generally did not participate in a social security programme providing old-age benefits. Traditionally, older persons worked as long as they were able. Those no longer able to work lived with their children or received financial support from their children, with the support in China traditionally coming primarily from sons.

In countries such as China, however, where birth rates have fallen rapidly and where many adult children in rural areas are moving to urban areas to work, the traditional support system for older persons may be weakening. As evidence of this, it has been found that families in rural China with fewer children and with fewer sons tend to save more for their retirement (Ebenstein and Leung, 2010). These changes increase the need for extending social security old-age benefit coverage to people living in rural areas.

In late 2009 China launched an innovative programme – the National Rural Pension Scheme – for rural residents. This programme is a major development in the provision of pensions in China. It has features – including, among others, voluntary membership, a single contribution per year, coverage for the parents of contributing participants, and contribution payments subsidized by government – that may provide lessons for other countries wishing to extend pension coverage to the rural and informal sectors. While voluntary programmes often have limited impact, this programme is succeeding in enrolling large numbers of people. This article discusses that programme.

The rest of this article is structured as follows. First, as background, it provides demographic and economic statistics about China and then discusses characteristics of workers in rural areas in China. To help understand the context in which the new rural pension programme operates, it then provides an overview of old-age benefits programmes in China. Following that, an analysis of the features and sustainability of the new pension programme for rural residents is offered. To provide an international perspective, the discussion turns to a number of programmes in other countries which in some respects have similar features and may provide lessons for China. It also discusses possible lessons for other countries from China’s experience. Lastly, possible changes to the rural pension programme are considered, followed by concluding comments.

**China: Demographic and economic background**

This section provides the demographic and economic background relevant for understanding China’s social security programmes. From 1990 to 2012, the total population in China increased from 1,143.3 million to 1,354.0 million (Table 1). Besides, the population is rapidly ageing. From 1990 to 2012, the ratio of
The ageing of the population is occurring to some extent because the total fertility rate is only 1.21 per cent and the natural rate of population growth is 0.5 per cent. The sex ratio at birth is 117.7 males per 100 females, a result in part of the preference for male children and the one child policy that was initiated in 1980 (National Bureau of Statistics of China, 2013). Life expectancy at birth increased from 68.6 years in 1990 to 74.8 years in 2010. In urban areas it is higher than the national average. By the end of 2010, it was 80.2 years in Beijing and 80.3 years in Shanghai (National Bureau of Statistics of China, 2012).

In China, all people are registered (Hukou system) as being either in the urban or rural sector. Since the 1990s, China has experienced rapid urbanization, which is creating challenges for the registration system. According to the statistics presented in the China Statistical Yearbook (see Table 2), the urbanization rate (percentage of the population with urban registration) increased from 26.4 per cent in 1990 to 52.6 per cent by the end of 2012, which means that the population aged 0 to 14 to the total population decreased from 27.7 per cent to 16.5 per cent, while the proportion of population aged 65+ increased from 5.6 per cent to 9.4 per cent. According to demographic projections, by 2030 the population aged 65+ will be 16.2 per cent, and by 2040 it will increase to 22.2 per cent (OECD, 2009).

Partly because of the migration of younger workers to urban areas, the old-age dependency ratio is higher in rural than in urban areas, with the difference projected to grow considerably in the future. It is predicted that the gap in old-age dependency ratios between rural and urban areas will widen from 4.5 per cent in 2008 to over 13 per cent by 2030, when the old-age dependency ratio will reach over one third in rural areas and 21 per cent in urban areas (World Bank, 2012).

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in urban areas outweighs the population in rural areas.\footnote{Usually, the urbanization rate would be measured as the percentage of the population living in urban areas. But when the urbanization rate is calculated in China, the rural population and the urban population refer to those residents with rural and urban registration, respectively. The urban population does not include the population that lives in the urban areas with rural registration.} By the end of 2012, about 711.8 million people had urban registration and 642.2 million had rural registration.

In China, nominal GDP per capita was CNY 38,355 by the end of 2012 and the GDP growth rate of that year was 7.8 per cent. Agriculture accounted for an estimated 10.1 per cent of GDP in 2012. China had reserves of foreign exchange and gold in 2012 of USD 3.3 trillion, which is the largest in the world (National Bureau of Statistics of China, 2013). The per capita disposable income of rural residents and urban residents in 2012 was CNY 7,917 and CNY 24,565, respectively. An estimated 13 per cent of the population live in conditions of poverty, and older persons in rural areas have higher poverty rates than urban workers, rural workers and urban retirees (Cai et al., 2012). The unemployment rate in 2012 was 4.1 per cent (National Bureau of Statistics of China, 2013).

### Characteristics of workers in rural areas in China

This section looks at the main contributors to, and participants in, the National Rural Pension Scheme: rural workers. Workers in rural areas in China share some characteristics in common with workers in rural areas in other middle- and lower-income countries. Having relatively low incomes compared to workers in urban areas in general, they earn income mainly by selling products produced on

<table>
<thead>
<tr>
<th>Year</th>
<th>Urban population</th>
<th>Rural population</th>
<th>Total population</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>million per cent</td>
<td>million per cent</td>
<td>million</td>
</tr>
<tr>
<td>1990</td>
<td>302.0 26.4</td>
<td>841.4 73.6</td>
<td>1,143.3</td>
</tr>
<tr>
<td>2000</td>
<td>459.1 36.2</td>
<td>808.4 63.8</td>
<td>1,267.4</td>
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<tr>
<td>2010</td>
<td>669.8 50.0</td>
<td>671.1 50.1</td>
<td>1,340.9</td>
</tr>
<tr>
<td>2011</td>
<td>690.8 51.3</td>
<td>656.6 48.7</td>
<td>1,347.4</td>
</tr>
<tr>
<td>2012</td>
<td>711.8 52.6</td>
<td>642.2 47.4</td>
<td>1,354.0</td>
</tr>
</tbody>
</table>

Note: Urban population and rural population in this table refer to number of people with urban registration and rural registration, respectively.

farmland and do not pay income taxes, while workers in urban areas generally do pay income taxes. Thus rural workers have no tax incentive to participate in social security or pension programmes.

Rural workers do not work only in agriculture; they may also work in other occupations, such as in small stores. The rural elderly depend far more than do the urban elderly on continued work in old age. Many rural workers continue working into their 70s, but income from work declines sharply for workers during their 60s. Family support becomes increasingly important as the elderly age (Cai et al., 2012).

For many rural families, the adult children are moving to urban areas to work. Many workers who are registered as part of the rural population have migrated to urban areas: the total number of people who live in areas other than their place of registration had reached 279 million by the end of 2012 (National Bureau of Statistics of China, 2013). The process of mass rural-to-urban migration can be seen in the rapid shift in living arrangements in rural areas, where the co-residence of rural elderly persons with their adult children fell from 70 per cent in 1991 to 40 per cent by 2006 (World Bank, 2012).

Differing from many countries, workers in rural areas in China commonly have bank accounts, which play an important role in the delivery of old-age benefits. Also, China has a strong culture of saving in banks, which is not present in many countries. This form of savings has in the past served as a substitute for financial savings through pensions. The average deposit level is high when compared to the average disposable income level in China. By the end of 2010, the average bank deposit amount of rural and urban residents counted together was CYN 13,305 per capita (National Bureau of Statistics of China, 2013). Individual savings thus play an important role in guaranteeing basic income security in old age.

Overview of social security old-age benefits programmes in China

China has three main social security old-age benefit programmes, covering three different groups of people. Urban areas have two old-age benefit programmes – the Urban Employees’ Pension Programme and the Urban Residents’ Pension Programme. The former is for people who have a formal job in urban areas with rural or urban registration, and the latter, started in 2011, is for people with urban registration who do not have a job. The National Rural Pension Scheme, which is the focus of this article, is for most people with rural registration.

2. In 2013, CYN 1,000 = USD 160 approx.
3. We use the term Urban Residents’ Pension Programme in this article as it is terminology used in Chinese policy regulation. Actually, the Programme was established for people with urban registration that are not employed.
National Rural Pension Scheme (NRPS)

Before 2009, relatively few people in rural areas qualified for a pension in old age (Yang, Williamson and Shen, 2009). In late 2009 China established the National Rural Pension Scheme (see Table 3), launching the programme in more than 300 counties on a pilot basis. The programme reached 23 per cent of counties by the end of 2010 (Mu, 2010), 60 per cent of counties by the end of 2011, and was expected to be operational in all counties by the end of 2012 (Yang, 2012). The scheme is sponsored by central government and run by the county or municipal government, with oversight from the Ministry of Human Resources and Social Security. Another voluntary national pension scheme for rural residents preceded this programme, but the contribution level and benefit level were low, the programme was not subsidized by the government, and the programme was not successful in covering a substantial portion of rural residents. The launch of the current programme was preceded by a period during which different pension arrangements were tried on a pilot basis in different parts of the country in an attempt to see which arrangement would work best (Cai et al., 2012).

Although the NRPS is structured as one scheme, it has two parts providing benefits to two different groups under different but related arrangements. The first

<table>
<thead>
<tr>
<th>Feature</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimum contribution</td>
<td>CYN 100 a year, made as a single payment; higher in some provinces</td>
</tr>
<tr>
<td>Maximum contribution, central government rules</td>
<td>CYN 500 a year; higher in some provinces</td>
</tr>
<tr>
<td>Age of benefit entitlement</td>
<td>60 (men and women)</td>
</tr>
<tr>
<td>Flat benefit</td>
<td>CYN 55 a month; higher in some provinces</td>
</tr>
<tr>
<td>Average benefit for persons aged 60+</td>
<td>CYN 74 a month</td>
</tr>
<tr>
<td>Number of years for vesting</td>
<td>15 years of contributions</td>
</tr>
<tr>
<td>Per cent of counties covered at the end of 2011</td>
<td>60 per cent</td>
</tr>
<tr>
<td>Per cent of counties expected to be covered at the end of 2012</td>
<td>100 per cent</td>
</tr>
</tbody>
</table>

Sources: Mu (2010); Yang (2012).

4. Some translations refer to the NRPS as the National Rural Pension “Plan”.
5. The Chinese population aged 60+ was 193.9 million and accounted for 14.3 per cent of the total population by the end of 2012. China is therefore home to approximately 21 per cent of the world’s 60+ population (UNDESA, 2007). Thus, social security old-age benefits programmes in China play an important global role in providing benefits for older persons. In turn, given that about 70 per cent of China’s population aged 60+ live in rural areas, about 14 per cent of the world’s population aged 60+ is covered by China’s National Rural Pension Scheme.
part is a contributory scheme – participants must contribute in order to receive benefits when they reach age 60. The second is a non-contributory scheme for people who are currently aged 60+. The relationship between the two parts of the rural scheme is explained below.

Coverage. All people with rural registration aged 16+, who are not students and who do not participate in another pension plan, can voluntarily participate in the NRPS. They can participate whether they work in a rural or urban area, whether they are employed or self-employed, and whether they work for pay or are in non-remunerated work. As shown in Table 4, participation in the scheme had grown from 103 million in 2010 to 483.7 million in 2012, with benefit recipients growing from 28.9 million to 133.8 million. The ratio of beneficiaries witnessed small variations from 2010 to 2012 (around 28 per cent).

Contributions. Contributions to the scheme are not calculated on the basis of earnings and anyone meeting the age requirements can contribute. The central government has established minimum levels for contributions at CYN 100 a year. The lowest maximum contribution, set by the central government, is CYN 500 a year (approx. USD 80 in 2013), with only 5 per cent of participants contributing that amount (Dorfman et al., 2013b). Each county can decide the exact contribution range applying in its jurisdiction (Gao, Su and Gao, 2012).

Chinese residents in rural areas who choose to participate must register at their village government office, the lowest level of the hierarchy of government. It is to this office that they pay the entire contribution for the year as a single cash payment. At the end of the contribution period (month), the village government aggregates all the contributions and transfers these to the township government, which in turn transfers the contributions of all villages to the county government. Depending on local regulations, the rural pension fund generally is managed by

Table 4. Coverage of the National Rural Pension Scheme, 2010-2012

<table>
<thead>
<tr>
<th>Year</th>
<th>Total participants</th>
<th>Contributors</th>
<th>Beneficiaries</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>million</td>
<td>million</td>
<td>per cent</td>
</tr>
<tr>
<td>2010</td>
<td>103.0</td>
<td>74.1</td>
<td>72.0</td>
</tr>
<tr>
<td>2011</td>
<td>326.0</td>
<td>237.0</td>
<td>72.7</td>
</tr>
<tr>
<td>2012</td>
<td>483.7</td>
<td>349.9</td>
<td>72.3</td>
</tr>
</tbody>
</table>

Note: Data for 2012 includes both participants of the National Rural Pension Scheme and the Urban Residents’ Pension Programme.


6. From lowest to highest, the levels of government in China are village government, township government, county government, municipal government, provincial government and central government.
the county government, but in some cities the municipal government is responsible. The future intention of central government is for the funds to be managed by provincial governments (Cai et al., 2012). Currently, the money is deposited in banks. The administrative expenses for the scheme are paid directly by local governments, which is a form of subsidy for the programme. Those expenses thus are not taken out of the contributions, which would reduce the amount of benefits.

**Eligibility.** Participants must contribute for 15 years in order to vest and be eligible to receive benefits at age 60. For participants who were older than age 45 when joining the scheme, to qualify for benefits they will have to contribute every year up to age 60 and then make a lump-sum payment to cover the shortfall in years (Cai et al., 2012).

**Benefits.** The benefits for participants who have contributed a minimum of 15 years comprise two components. First, a basic benefit that is not means tested and is not financed by the contributions of participants. Persons who are aged 60+ can receive the basic benefit of CYN 55 a month if they are not receiving another pension and all their children are contributing to the rural pension scheme, regardless of whether the children are working. This amount equated to one tenth of the average monthly wage in rural areas in 2011 (Wang and Qing, 2012). This benefit represents the first time that the Chinese government has made a major financial commitment to a rural pension system (Shen and Williamson, 2010). The benefit will be adjusted for inflation, but the exact adjustment mechanism has not yet been determined (Cai et al., 2012).

In addition, a defined contribution benefit is provided based on the accumulation in the participant’s individual account from the participant’s contributions and accrued investment returns. That benefit is paid monthly and equals the individual account at age 60 divided by 139, which is the same factor used for calculating monthly pensions from the individual accounts in the urban scheme. Persons do not need to stop working to receive this benefit. The benefit payment is not limited to the amount in the individual account, but is guaranteed by the government for life, and thus is paid as an annuity. If the person dies before receiving the full amount in their personal account, the spouse receives the remaining amount; or the children in cases where the spouse is also deceased.

**Urban Employees’ Pension Programme (UEPP)**

Launched in 1984, the UEPP covers employed workers in urban areas. At present, government agencies and public institutions are not covered.

**Coverage.** As shown in Table 5, participation has grown from 61.7 million employees in 1990 to 304.3 million employees in 2012, with beneficiaries accounting
for 9.7 million and 74.5 million of these totals, respectively (National Bureau of Statistics of China, 2013). The proportion of beneficiaries among the total number of participants increased from 15.7 per cent in 1990 to 24.5 per cent in 2012.

**Contributions.** The contribution rate is 28 per cent of wages, of which the employee contributes 8 per cent to an individual account and the employer contributes 20 per cent to the social account for the basic pension. The contribution rates of 8 per cent plus 20 per cent are standards suggested by the central government, but the exact contribution rates can be decided by local government, and can be higher or lower. The contribution rates of Guangzhou city are 12 per cent for the social account and 8 per cent for the individual account, and they are contributed by employers and employees, respectively. Guangzhou has a considerably lower contribution rate for the social account because many younger migrants live in the city, so population ageing is less marked in this city. The contribution rates in Beijing are 20 per cent for the social account plus 8 per cent for the individual account. In Shanghai, which faces serious population ageing, the respective contribution rates in Shanghai are 22 per cent and 8 per cent. The 8 per cent contribution rate that workers make for the individual account does not vary across provinces, because the account is linked to the individual participant and is not affected by the province’s age structure.

**Eligibility.** Workers must have 15 years of credits, based on years of contributions, to be eligible for monthly benefits when they retire. The retirement age is 60 for men and women working in certain professions, 55 for female managers, and 50 for other women. The retirement age is lower for those working in hazardous occupations.

### Table 5. Coverage of the Urban Employees’ Pension Programme, 1990–2012

<table>
<thead>
<tr>
<th>Year</th>
<th>Total participants Million</th>
<th>Contributors Million</th>
<th>Per cent</th>
<th>Beneficiaries Million</th>
<th>Per cent</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>61.7</td>
<td>52.0</td>
<td>84.3</td>
<td>9.7</td>
<td>15.7</td>
</tr>
<tr>
<td>2000</td>
<td>136.2</td>
<td>104.5</td>
<td>76.7</td>
<td>31.7</td>
<td>23.3</td>
</tr>
<tr>
<td>2010</td>
<td>257.1</td>
<td>194.0</td>
<td>75.5</td>
<td>63.0</td>
<td>24.5</td>
</tr>
<tr>
<td>2011</td>
<td>283.9</td>
<td>215.7</td>
<td>76.0</td>
<td>68.3</td>
<td>24.1</td>
</tr>
<tr>
<td>2012</td>
<td>304.3</td>
<td>229.8</td>
<td>75.5</td>
<td>74.5</td>
<td>24.5</td>
</tr>
</tbody>
</table>

**Benefits.** The retirement benefit consists of two parts: a basic benefit and an individual account benefit. The basic benefit is calculated by multiplying the following two elements: i) a percentage determined by total contribution years, where one contribution year equals 1 per cent; ii) the average of the social average wage of the year prior to the employee’s retirement age and the indexed wage of the employee. The social average wage used in this calculation is the average wage for the pooling area where the worker resides at the time of retirement.

The monthly benefit based on the individual account is the balance in the worker’s individual account balance at the time of retirement divided by 139. Once benefit payments have started for a worker, initial retirement benefits are adjusted each year by an amount established annually by each provincial government. The adjustment is intended to take into account changes in wage and price levels and the financial health of the programme. There is no set formula for calculating the amount of the adjustment and it need not be the same in every province. According to statistics produced by the Ministry of Human Resources and Social Security (2012), the average monthly UEPP benefit level at the end of 2011 was CYN 1,721.

*Urban Residents’ Pension Programme (URPP)*

Launched in 2011, the URPP is a subsidized voluntary programme covering people with urban registration who do not have a job.

**Coverage.** By the end of 2011, 5.39 million people participated in the URPP, of which 2.35 million were beneficiaries (Ministry of Human Resources and Social Security, 2012).

**Contributions.** The annual contribution amount regulated by the central government varies from CYN 100 to CYN 1,000, divided into 10 levels by increments of 100. Participants can choose the contribution level. However, because the URPP is managed by the county or municipal government, the range of choice of contribution levels differs between areas. Local governments subsidize those who participate. The lowest subsidy level is CYN 30 per participant per year. Local governments can raise the subsidy level according to the health of their finances.

**Eligibility.** To receive monthly benefits, the participant must have 15 years of credits and be of retirement age. Those persons aged 60+ can receive the basic benefit from government without having contributed.

**Benefits.** These comprise two parts. One is the non-contributory benefit – CYN 55 per person per month (local governments can raise the non-contributory benefit level according to the health of their finances). The other comes from the person’s individual account, which depends on the contribution level of the participant.
The governments pay the cost of the non-contributory benefit. In the richer and eastern provinces of China, the central government subsidizes 50 per cent of the non-contributory benefit, and the local government pays the remaining 50 per cent. In the poorer middle and western provinces, the central government pays 100 per cent of the benefit, removing the need for a subsidy paid by local government.

**Features and sustainability of the NRPS**

The NRPS differs from the UEPP and the URPP in important aspects such as contribution level, government subsidy, benefit age and benefit level. In what follows we analyse the NRPS’s main features and the issue of its sustainability.

**Government subsidy and participation incentives**

Central government and local governments play an important role in the NRPS contribution and benefit payment process (Table 6). Local government provides a flat matching contribution to encourage rural residents to participate. The government matching contribution and the person’s contribution are paid into the person’s individual account. The contribution subsidy is CYN 30 a year, where the minimum contribution set by the central government is CYN 100 a year (approx. USD 16 in 2013). The lack of a tax incentive for rural residents to participate may explain in some measure the matching contribution. The government subsidy presumably improves the participation rate of the rural population in this scheme. Moreover, as participants younger than age 60 have to contribute for at least 15 years to receive a benefit, the government’s continued subsidy represents an incentive for the continued payment of contributions by participants beyond 15 years.

However, some commentators have argued that the matching contribution is too low to be effective in encouraging participation (Cai et al., 2012). Besides, the flat matching contribution does not act as a strong incentive for participants to

| Table 6. Government subsidy for participants of the National Rural Pension Scheme |
|---|---|---|
| Process | Contribution | Benefit payment |
| Subsidy object | Personal account | Basic benefit |
| All areas | Eastern areas | Central and western areas |
| Subsidy level | Local government subsidizes CYN 30 per year per capita | Local and central government pay 50 per cent of basic benefits respectively | Central government pays 100 per cent of basic benefits |

pay a higher level of contribution. No matter the contribution level chosen by participants, they receive the same level of government subsidy. Thus, nearly half of participants make the minimum contribution (Dorfman et al., 2013a and 2013b).

Further, the incentives to rural residents to participate differ greatly at different ages. A person who is more than 15 years from benefit entitlement and whose parents are still working, has little incentive to participate. However, if the person’s parents are aged 60+ the incentive is large. The requirement that all the recipient’s children contribute is called “family binding”. This incentive may work particularly well in China, which has a strong tradition of adult children taking care of their older parents. If a participant contributes CYN 100 a year, and if his or her siblings do also, the parents can receive CYN 55 a month; or CYN 110 a month (CYN 1,320 a year) for a married couple. If older persons do not have children, they automatically qualify. The “family binding” requirement on the adult children to contribute is made by the central government, but enforcement is a local-level responsibility. At the local level, however, the incentive to receive the central government subsidy for benefits for people aged 60+ works against the strict enforcement of this requirement, so that some local governments may qualify all persons aged 60+. In light of this generous arrangement, and perhaps because of lax enforcement of the “family binding” requirement, it appears that most elderly persons in rural areas are receiving benefits.

In eastern areas of China, local government and central government evenly share the cost of paying the basic benefit. By contrast, in central and western areas, the central government pays 100 per cent of the basic benefit. These differences occur mainly because local governments in eastern areas can bear this share of the cost. Policy simulation shows that both central government and local government can afford to finance the basic benefit.7

Contribution level and benefit level variations

While most small counties use the government minimum standards (CYN 100 to CYN 500 a year, with CYN 100 increments) for contribution levels, variation above those standards is permitted and occurs in some counties and cities that have a higher standard of living. As examples of regional variation in contribution levels, in Wuhan city the minimum annual contribution is CYN 200 and the maximum annual contribution is CYN 1,200, while in Shanghai the minimum and maximum annual contributions are CYN 500 and CYN 1,300 respectively. In both Wuhan

7. Projections suggest that the proportion of annual central government financial subsidy to annual central government fiscal revenue varies from 1.2 per cent to 1.5 per cent from 2010 to 2053; the corresponding proportion of local government financial subsidy to annual local government fiscal revenue varies from 0.1 per cent to 0.7 per cent (Xue, 2012).
and Shanghai, increases in contributions are permissible between the minimum and maximum amounts in CYN 200 increments. In some prosperous provinces, maximum contributions of up to CYN 2,500 are permitted (Cai et al., 2012). For all areas, levels of contributions will be adjusted upward over time to reflect increases in income.

The regional variation in contribution levels is set at the level of the provincial government. China has 33 provincial-level governments; Beijing, Shanghai, Chongqing and Tianjin are four municipalities that are treated as provinces. Besides, two Special Administrative Regions (Hong Kong and Macao) are treated as provincial governments. Also, the responsibility for paying contributions is divided among provincial, municipal, and county governments, and the exact per cent sharing by different levels of local governments differs in different provinces.

Unlike most national social security programmes, in China, social security benefit financing differs by region and it also involves financing in part by local governments. Localities can increase the benefit amount above CYN 55 a month if they have the financial resources to do so. The average benefit received by beneficiaries is CYN 74 a month (Yang, 2012).

A comparison of two localities provides an indication of the degree of variation in benefit levels across regions. If a participant from a small village in the suburbs of Beijing, which is a relatively high-income area, joins the pension scheme at age 20, when he or she reaches age 60, a monthly benefit of around CYN 270 will be paid from his or her personal account plus a government subsidy of CYN 280 per month through the basic benefit, as well as other bonuses. In total he or she will receive about CYN 600 per month (Yang, 2012). By contrast, in some districts of Wuhan city, those rural residents who are aged 60+ receive the basic non-contributory benefit (CYN 100 per month or CYN 1,200 per year). The basic benefit is not enough to meet the basic living needs of the elderly, especially in developed areas. For instance, the average per capita expenditure for food by rural residents in Wuhan was CYN 3,068 per year in 2011 (Statistical Information of Wuhan, 2012).

Benefit age

Both men and women can receive benefits from the NRPS at age 60. By contrast, although the retirement age is 60 for men and women who work in certain professions, it is age 55 for female managers and age 50 for other women covered by the UEPP. Also, these ages for benefit receipt are the mandatory retirement ages for most urban workers. Only a small percentage of urban workers are exempt from these requirements, for example some university professors. In addition, workers in hazardous or dangerous occupations can qualify for benefits up to 5 years earlier than these ages. The exception provided for workers in hazardous or
dangerous occupations does not apply to workers covered by the NRPS. Research suggests that the effective retirement age in urban areas, for men and women combined, is age 53 (Sin, 2005), while in rural areas benefits cannot be received until age 60. The benefit eligibility age in the NRPS is thus considerably higher than in the urban pension system.

The 10-year difference (age 50 versus age 60) in the age of entitlement to benefits for women covered by the NRPS compared to those covered by the urban pension system is not justified by a difference in life expectancy. People in rural areas have lower incomes than people in urban areas, and presumably also have lower life expectancies. Clearly, the higher pension age in the NRPS makes the rural pension system less costly than the UEPS. However, the NRPS retirement age of 60 is actually in keeping with current practice in other countries, more so than are the early retirement ages in the UEPS. It is in line with a global trend to raise the retirement age for women to equal that of men.8

Financing issues

Currently, the NRPS is performing well from a financial perspective. As shown in Table 7, from 2010 to 2012, the revenue, balance (difference between revenue and expenditure), and accumulation of this scheme increased significantly.

The divisor of 139 is the key parameter in determining the generosity of the individual account benefit. Thus, in assessing the financing of those benefits, it is important to determine whether that divisor provides benefits that are adequately financed, or alternatively, whether the benefits are overly generous. When financial planners in the United States advise individual account holders as to the sustainable amount that a retiree can withdraw from an account without overly risking that they will run out of money, they often advise that a retiree can withdraw 4 per cent of the initial account balance, adjusted for inflation, each year (McKenzie and Turner, 2012). That advice depends on the life expectancy of the individual and the expected rate of return received on the account. It would be a lower percentage for longer life expectancy and a lower expected rate of

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8. For a discussion of this trend in OECD countries, see Turner (2007).
return. In China, the life expectancy at older ages is shorter than in the United States, but the expected rate of return is also lower, with the two factors having effects that offset to some extent.

The divisor of 139 for monthly benefits is equivalent to a divisor of 11.6 for annual benefits, which is equivalent to withdrawing 8.6 per cent of the initial account balance each year. Thus, it appears that the benefit divisor of 139 should be increased if the goal is to have a system that is financed primarily by the contributions of participants. That change would result in lower benefits, but would be more consistent with a sustainable, self-funding pension system. By one analysis, county governments will be liable for 40 per cent of the payments from the individual account pensions (Herd, Hu and Koen, 2010).

The experience with the urban pension system may provide lessons for the rural pension system with respect to the financing of the individual accounts. The pension for persons in urban areas also has the twin features of a basic benefit and a contributory individual account. However, the government has not segregated the money in the individual accounts from other social security funds, and has in fact spent much of the funds in the individual accounts, now in essence converting those accounts to notional accounts to which interest is credited (The Economist, 2012).

The government could contribute to the social account for a rural resident a total of CYN 450 over 15 years (CYN 30 a year) and that person receive the basic benefit, financed by the county government, of CYN 660 a year (CYN 55 a month), starting at age 60. Thus, the “break even” point, where the participant had received as much in benefits as the government had contributed, would occur in less than a year. This calculation indicates that the government heavily subsidizes the basic benefit beyond the government’s initial contribution of CYN 30 per year. Thus, the benefit is not advanced funded, but will require government subsidies in the future when those benefits are paid.

In 2011, 61 per cent of the total revenue for the rural pension system came from government subsidies (Wang and Qing, 2012). This figure presumably will rise in the future as more participants eventually qualify to receive benefits. The individual pays for none of the basic benefit for parents and for none of his or her own basic benefit. The cost to the central government of providing the non-contributory benefit to all the 100 million rural persons currently aged 60+ would be about 2 per cent of the government budget (Shen and Williamson, 2010). This percentage presumably will decline over time as the current cohort of retirees who are receiving non-contributory benefits will gradually be replaced by a cohort of retirees that will be receiving benefits from the new contributory programme. The basic benefit the new cohort receives will still be entirely financed by the government, but that financing will presumably come in part from the amount currently being contributed by the government to meet that future expense.
The government also subsidizes a substantial portion of the individual account benefit. This cost is borne by local governments. Local governments differ considerably in their level of economic development, and thus their ability to bear this cost. Overall, individual contributors will only pay at most 18 per cent of the cost of their pensions, with the government paying the rest (Herd, Hu and Koen, 2010).

The government is thus incurring what appear to be substantial unfunded liabilities for the rural pension system. In addition, it has substantial unfunded liabilities for the urban pension system (Reuters, 2012). Thus, it appears that reforms may be needed in these systems to reduce their liabilities and increase their revenues. The central government has large non-pension reserves that could be used in the future to help pay for these liabilities (The Economist, 2012).

In comparison to programmes in other countries, the total cost of the rural pension programme in China is relatively low at 0.22 per cent of GDP. This compares, for example, to 0.38 per cent of GDP for a means-tested programme in Chile (Herd, Hu and Koen, 2010). Thus, the programme combines a relative low cost, due to low benefits, and a high degree of government subsidy, due to the relatively small amount contributed by participants.

In China, the rate of return on provincial urban pension funds has averaged 2 per cent over the last 10 years, which is less than the rate of inflation over that period. However, in 2012 the national government announced a pilot programme that would permit the 13 provinces that manage pension funds for individual accounts to invest in domestic equities. The Council that manages the National Social Security Fund, which is China’s public pension reserve fund, will act as the trustee and principal investor of each of these funds. The National Social Security Fund was established in 2000 to support China’s future social security expenditures. The amount invested this way could be as much as CYN 360 billion (approx. USD 57 billion), roughly 20 per cent of the funds’ combined total assets under management (SSA, 2012).

**International comparisons**

In order to place China’s new social security programme for rural workers in a broader perspective, this section presents international comparisons with benefit programmes that are similar in some aspects to the NRPS.

*Comparison with unemployment insurance in the United States*

Some of the complexities of the Chinese pension system arise due to regional differences in the programme. Those regional differences may be understood by recognizing that they have some similarities to the unemployment insurance...
system in the United States. While that is not a pension programme, it shares the similarity with the NRPS in China in that it differs across the states.

In the United States, unemployment insurance is based on a dual programme of federal and state laws. Each state administers a separate unemployment insurance programme, which must be approved by the Secretary of Labor (federal government), based on federal standards. A combination of federal and state law determine which employees are eligible for compensation, the amount they receive, and the period of time benefits are paid (Legal Information Institute, 2012).

Comparison with the Mbao Pension Plan in Kenya

In some countries, voluntary pension systems have been provided to informal sector workers as a substitute for mandatory social security programmes. Both the NRPS in China and the Mbao Pension Plan in Kenya are new, innovative pension plans that are succeeding in enrolling rural or informal-sector workers (Kwena and Turner, 2013). Both are voluntary plans for persons who typically do not pay income taxes, and thus do not have a tax incentive to participate. In both plans, contributions are not tied to earnings, and participants can determine the amount of their contributions, within limits.

Both have innovative approaches for dealing with small contributions, but their approaches can be considered to be exact opposites. In Kenya, participants can make numerous small contributions of as little as the equivalent of USD 0.25. In China, participants make a single annual contribution equivalent to as little as USD 16.00. Both plans have extra incentives for participating. In Kenya, workers can use their pension account as security for obtaining a mortgage for purchasing a house.

Comparison with pension programmes for rural workers in other countries

The contributory part of the NRPS has similarities to programmes for rural workers in some other countries. Extending social security programmes from the formal sector to the informal sector often does not work. This is partly because contribution rates, which may be reasonable for the formal sector, often appear to be too high a hurdle for participation in social security for workers in the informal sector. For this reason, some countries have separate programmes with lower contribution rates for the informal sector. In Tunisia, for example, agricultural workers have a lower contribution rate than urban workers. In the past, efforts to extend coverage to the informal sector have relied on a tax being levied based on some assessment of the earnings of those workers. The new programme in China differs
from past efforts in most other countries in that it is not tied to the earnings of workers.

Another trend in providing pensions for low-income persons in old age is to provide non-contributory pensions. The non-contributory benefit for older persons and the basic benefit part of the contributory programme in China have similarities with some programmes for rural workers in other countries. A number of middle- and lower-income countries have established non-contributory, often means-tested, old-age pensions to provide benefits to poor people in old age and to extend the coverage of social security programmes (ILO, 2010). This trend has been motivated by an attempt to reduce poverty in old age and appears to be gaining greater acceptance around the world. These programmes are sometimes called social pensions. Countries with social pensions include Botswana, Brazil, India, Lesotho, Mauritius, Namibia, Nepal, and South Africa. Chile adopted such a programme in 2008, and also established a minimum benefit for participants who had contributed to the mandatory individual accounts and met certain other requirements. In 2008, Belize extended to indigent older men its non-contributory poverty programme that already applied for indigent older women. The Maldives adopted a programme in 2010. Peru and the Philippines both adopted programmes in 2011 (Turner and Rajnes, 2014). The non-contributory pension for older persons in China is similar in some respects to a social pension, but it differs in that it requires the contributions of children and it is not means tested.

Possible lessons for other countries

The NRPS has several innovative features that could provide a model for other countries seeking to extend old-age benefit coverage to workers in the rural and informal sectors. It is a voluntary programme, but it encourages coverage of workers who do not pay income taxes, and thus have no tax incentive to participate, through the provision of government subsidies. As a further incentive, old-age benefits are provided to the parents of participants who contribute, when all the adult children in a family are participating in the contributory programme.

An important feature of the NRPS is that the contribution rate is much lower than in the programme for urban workers, where the rate is 28 per cent of pay. The NRPS contribution is made by the individual, supported by a matching contribution made by government, with no contribution by employers. The programme covers self-employed workers and also non-workers.9

The NRPS provides a redistributive benefit, which is a flat-rate benefit, and a contributions-related benefit. To facilitate contributions, it requires only a single

9. The term “non-worker” includes those persons engaged in non-remunerated forms of work.
contribution per year. The government provides a guarantee for benefits, so that individuals will continue to receive benefits even if they have exhausted the amount in their individual account. The government essentially annuitizes the individual account at a generous rate. This guarantee will require subsidies by the government.

Assessment and possible future changes in China

In particular because the social security programme for rural residents in China is so new, it can be expected that over time changes will be made to improve its functioning. Even though the system has grown rapidly, some aspects of its design have kept levels of participation below what it otherwise might have been. Although many people in rural areas may not be well informed about the NRPS, a disincentive for those who do know about it is that the assets in the system are invested entirely in one-year government bonds, which provide a rate of return that is less than the rate of inflation. In this respect, the participants in the system provide a reverse subsidy from participants to the government, but this reverse subsidy is more than offset by government subsidies for benefits. A more transparent arrangement might be to raise the interest rate on the assets in which the system invests, but also at the same time raise the contributions required of participants. An increase in participant contributions would help with the sustainability of the system, but would need to be balanced with the desire to have a high level of participation in a voluntary system. In addition, some rural residents may have chosen not to participate because they mistrust government programmes, suggesting a need to develop a strategy to encourage greater trust in the NRPS.

A possible change in financing would be to shift the burden from county governments to the central government, to reduce the burden on lower-income parts of the country. Specifically, rural areas are set to age at a greater rate than urban areas, so the burden of ageing would be shared more evenly across the country (Herd, Hu and Koen, 2010).

A change that has been discussed in China is combining the three different social security old-age benefit programmes. An intermediate change would be to facilitate the transfer of contributions and credits of years toward vesting between the three programmes. In 2011, a law was passed to facilitate workers relocating to different geographical areas by allowing them to transfer their accrued rights to the programme in the new area of residence (SSA, 2011). Another possible change is that contributions could be permitted, or required, to be paid more frequently than once a year. The incentive structure would be improved if the basic benefit of CYN 55 a month was increased for years of contributions beyond 15. For example, it might be increased by CYN 3 a month for each additional year of contributions.
so that a person who had contributed for 16 years would receive an additional CYN 3 a month, for a basic monthly benefit of CYN 58.

At some point in the future, a possible change would be to allow participants who wished to do so to choose the investments for their individual accounts. Making this change, however, would then raise issues concerning financial literacy that have arisen in other countries where workers choose the investments for the funds held in their individual accounts (Turner and Muir, 2013).

Recognizing that China’s economic success will enable continuing improvements in life expectancy, a policy could be enacted so that future retirement ages for benefit receipt will be higher than those currently in use. This change might be enacted years in advance of its implementation to enable workers to plan for the change and designed so that it would only be applied if life expectancy increased as expected.

Conclusions

In late 2009 China launched an innovative programme, the National Rural Pension Scheme, which by 2011 had already extended pension coverage to more than 326.4 million rural residents, including contributors and beneficiaries. The NRPS is thus a major development in the provision of pensions in China. It combines a voluntary contributory programme for current participants and a non-contributory programme for the parents of those participants. The contributory programme provides a flat-rate benefit and a contributions-related benefit through an individual account.

The financing of the scheme varies across regions, with the central government providing all of the financing for the basic benefit in the central and western parts of the country, but only half of the financing (with local government providing the other half) in the more prosperous eastern provinces. The level of contributions made by participants and the level of benefits they receive also vary across regions. Albeit designed as a voluntary programme, it encourages coverage of workers who do not pay income taxes, and thus have no tax incentive to participate, by providing substantial government subsidies. Additionally, old-age benefits are provided to the parents of participants who contribute, when all the adult children in a family are participating in the contributory programme. To facilitate contributions, it requires only a single contribution per year. Participants can choose the level of contributions from a range, but allowing for a relatively small contribution.

While social security old-age benefit programmes are generally uniform national programmes, at least for the group of workers they cover, the NRPS in China has regional variations that make the programme more complex, but that also relate to regional differences in the country’s standard of living. Overall, its
features may provide lessons for other countries wishing to extend pension coverage to the rural and informal sectors.

**Bibliography**


Extending social security coverage to the rural sector in China


Abstract  To achieve national goals defined by the 1988 Brazilian Federal Constitution, cash benefits alone are insufficient in the absence of more robust social services to reduce inequalities and improve social cohesion. The Constitution, albeit of national importance and international significance, has not addressed many institutional and administrative weaknesses in the design of the national pension system. Although coverage has been increased and inequality reduced, these measures are not sufficient. Brazil’s ambitions to further develop social policies (and, indeed, to live up to its accorded international status as a social policy leader) may be constrained by an over-reliance on conditional cash transfers such as those provided under the Bolsa Família programme. Brazil faces a major political-economy challenge in addressing all these issues because the policy reform process is difficult, and, more importantly, because of the embedded role of vested interests. Moreover, Brazil must tackle these issues in the face of growing fiscal pressures, which could weaken the current political legitimacy of social policy and undermine important recent successes.

Keywords  pension scheme, social security planning, social security reform, Brazil
Introduction: The Brazilian pension model

With respect to pension provisions, Brazil has been an outlier in Latin America. While most of the larger countries in the region implemented paradigmatic reforms that featured defined contribution (DC) individual accounts to either substitute or complement public pay-as-you-go (PAYG) systems, Brazil instituted parametric reforms that emphasized fiscal transfers for lower-income workers, combining social insurance with social assistance pensions, as determined by the 1988 Federal Constitution (Chamber of Deputies, 2010).

The contrast in policy across the region became apparent in the 1980s and 1990s when high administrative and transaction costs associated with individual accounts led to projections of lower income replacement rates. Despite the movement towards DC pension systems, the hoped for positive impacts of rapid GDP growth, higher levels of investment and job formalization did not meet the earlier upbeat projections in countries such as Argentina, Chile or Mexico (Kritzer, Kay and Sinha, 2011).

Under these circumstances, Brazil’s social security system became something of a showcase, since fiscal transfers were generous in providing lifetime benefits. The combination in Brazil of a conventional defined benefit pension system and social assistance cash transfer benefits for the most vulnerable groups, along with high rates of coverage, received widespread popular support.

Nevertheless, the Brazilian model for old-age pensions and disability insurance, although successful in many respects, suffers from high levels of inefficiencies and requires careful critical analysis. In 2011, public expenditures on social policies amounted to 23 per cent of GDP, and pension benefits reached 14.5 per cent of GDP. The political debate over reform continues, but often lacks detailed analysis with respect to the distributional consequences and the extent to which the system favours the better off. Low levels of accountability and transparency with respect to public policy jeopardize what may be, in fact, an interim policy success story. That is to say, in the wake of challenges heightened after the 2007–08 global financial crisis and the rise of emerging economies that may not fully respect basic social rights as defined by International Labour Organization (ILO) Conventions and Recommendations on social security, there are new challenges.

This article focuses on pension policy within the context of Brazil’s social security system, and the need for a new reform agenda that emphasizes social rights that are consistent with the objective of sustained economic growth. Reforms that would ensure equitable and efficient pensions need not depend upon constitutional amendments, but can also be achieved through less onerous means such as ordinary legislation and administrative and institutional reform measures. The article is structured as follows: after a discussion of pension coverage, the performance and effectiveness of Brazil’s social security pension provisions are then
examined. We then examine Brazilian social security reform and conclude with policy proposals.

**Pensions in Brazil: The success of universal coverage**

Retirement coverage in Brazil can be traced back to the colonial period, when in 1554 the *Santa Casa de Misericórdia* in Santos first provided pensions. In 1919, after the formation of the International Labour Organization, workplace injury insurance was established and guided by new international recommendations. Social security legislation since 1919 reflects increasing state intervention, centralization, and universalization of coverage for workers in more precarious occupations – all of which was foreseen as early as 1945, but not enacted upon until the early 1970s. Initial regulations were tightly linked to Brazil’s labour code, but over time they have taken on their own juridical identity (Matijascic, 2002; Matijascic and Kay, 2008).

Current Brazilian social policy is based upon the Social Order section of the Constitution enacted in 1988 and regulated by Laws 8.212 and 8.213 from 1991 (workers in the private sector) and Law 8.112 from 1990 (federal civil servants) concerning pensions. The 1988 Constitution’s principal innovation was the creation of the concept of “social security”, a term intended to unify health, social assistance, unemployment and pension policies. Furthermore, it created the social security budget – which segregated funds from other public budget lines – with the intention that social security budget resources could only fund social security. The most significant changes with respect to coverage in the 1988 Constitution were:

- Utilizing the Brazilian minimum wage as the benefit floor;
- Establishing equivalent rules for urban and rural benefits; and
- Equalizing benefits for men and women.

The 1988 Constitution was, according to Werneck Vianna (1998), a reaction to the institutional model imposed after the 1964 military coup that deposed the President-elect, João Goulart. The range of reforms introduced between 1964 and 1968 sought to modernize the Brazilian State through public policies similar to those found in the leading Western economies. During that period, the military government instituted tax reform, created the Central Bank, and reformed social policies. The reforms sought to concentrate personal incomes in the upper income deciles to support stronger consumer spending, which was expected to lead to sustained economic growth, and thus higher per capita income that would progressively incorporate all of the population. Consumption was to be the driving force behind the Brazilian economy.

Social institutions were organized in order to provide protection for lower-income workers, with those seeking higher quality services expected to pay for private provision. This was the essence of the so-called conservative modernization.
of social policy. Since the cost of private provision was unaffordable for more than two-thirds of the labour force, the focus of the authors of the 1988 Constitution was to consolidate a system of universal protection through pensions, social assistance, health, and education with progressive improvement in quality (Werneck Vianna, 1998). It is important to note that this situation still persists, with only a minority of the Brazilian population obtaining health care, education, and pensions via market provisions.

The most salient result after the introduction of the new constitutional provisions was the expansion in the number of old-age benefits paid to rural workers and senior citizens living in households with income below a quarter of the minimum wage, an unofficial poverty line. For rural workers, the retirement age was 65, but after the Constitution of 1988 it was lowered to age 60 for men and age 55 for women. For the elderly in poverty, the age to receive benefits was lowered from age 70 to age 67 in 1996, and to age 65 in 2003 for men and women.

According to the 1988 Constitution, constitutional amendments1 require two voting rounds in the Chamber of Deputies and two voting rounds in the Senate, both of which require a minimum of 60 per cent of the votes cast. Any amendment introduced in the Senate requires two additional rounds of votes in the Chamber of Deputies.

Debate over pension reform has been centred upon parametric measures that focus on benefit rules and new forms of retrenchment. In 1998, a major reform included:

- Substituting length of service for length of the contribution period, with the introduction of the fator previdenciário (retirement factor), with rules similar to those of notional accounts;
- Fixing the minimum retirement age for new entrants to the public sector at age 60 for men and age 55 for women (ages 53 and 48, respectively, for those already working); and,
- New rules for disclosure, accountability, vesting, and portability of pension funds to stimulate defined contribution funds.

In 2003, a new pension system was established that would institute defined contribution plans for civil servants earning over the equivalent of USD 2,200 per month. Despite the approval of the constitutional amendment, the proposal received a great deal of opposition from the parties of the Left, and the law applies to those who have entered the civil service after February 2013. The 2003 reform introduced other relevant measures to link the value of the benefit to contributions, including the requirement that workers pay contributions on

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1. Reform of the pensionable age requires a constitutional amendment. See footnote 9 for an explanation of which types of social security reform require constitutional amendments.
benefits above the private-sector ceiling, which remains in effect despite judicial challenge (President Cardoso had been unsuccessful in his attempt to impose such a measure).

The 1998 and 2003 reforms were not trivial, raising requirements for accessing benefits and reducing replacement rates for workers in the public sector who have contributed for fewer years or who retire earlier than workers in the private sector. It is important to stress that the legislature refused to delink minimum benefits from the minimum wage or to remove the rules for National Institute of Social Security (Instituto Nacional do Seguro Social – INSS) benefits from the 1988 Constitution. The impact on coverage can be seen in Figure 1.

Figure 1 presents the most fundamental elements of social security in Brazil: the 1988 Constitution and the consolidation of democracy have resulted in improved access to benefits, but the number of contributing workers with guarantees of social rights is still low, having risen from 33 per cent in 1978 to 41 per cent in 2012. The number of workers without coverage has dropped from 48.2 per cent in 1978 to 31.2 per cent in 2012. In short, the 1988 Constitution guaranteed the rights of the more vulnerable sectors of the population and removed the stratification of the conservative modernization. As a result, there was a notable rise in coverage, but without a concomitant expansion of contributors: a mismatch that has had a significant impact on debates over reform.

Source: PNAD (annual household survey) for selected years.
The 1988 Constitution and its impact on the distribution of benefits and public policy performance

After being severely criticized for its levels of social inequality in the 1990s, as described by Matijascic (2002), Brazil has become a showcase for developing countries given its extension of coverage, including non-contributory benefits. The distribution of benefits illustrates the importance of providing old-age benefits according to the capacity to contribute (MPS, 2013; data from September 2013 that includes private-sector workers and workers in small-sized cities):

- 18.5 per cent were contributory benefits, with a contribution period of 30 to 35 years of contributions;
- 26.9 per cent are disability benefits;
- 9.5 per cent are benefits for attaining age 65 for male urban workers and age 60 for female urban workers, with a contribution period of 15 years;
- 15.6 per cent are for rural workers who have reached age 60 (men) and age 55 (women);
- 29.4 per cent of benefits are granted to workers older than age 65 or disabled persons with a family per capita income below one quarter of the national minimum wage.

Only 18.5 per cent of benefits are paid to persons that have contributed regularly. Those with partial contributions, that is to say, for persons receiving disability benefits or for urban workers granted old-age pensions, represent 36.4 per cent of benefits in payment. Those that contribute little or nothing, including rural workers and the poor, receive 45 per cent of benefits. To sum up, 81.5 per cent of Brazilians who receive a pension do not contribute regularly via payroll taxes. In this context of fragile labour markets and very high levels of precariousness, it is evident that tax transfers are essential to achieve universal coverage. The social security budget is responsible for this function.

Between 1978 and 2012 there was a substantial increase in the number of families with a member receiving a pension. In 1978, 8.3 per cent of families in the lowest income decile had a household member receiving a retirement pension compared to 60.1 per cent in 2012, while for the median and upper income deciles, the figures rose from 20.9 per cent and 20.7 per cent to 46.6 per cent and 46.8 per cent, respectively. The most substantial increase occurred among lower-income families. Improved access to non-contributory pensions, along with outreach efforts, were essential for increasing the number of families receiving old-age benefits. In order to measure the impact of old-age benefits on family income, Table 1 quantifies the role played in family income by social security cash benefits.

The increase in the number of people across all income deciles living in households who receive old-age benefits is matched by a considerable increase in
retirement and social assistance pensions. The data presented in Table 1 shows the change after the introduction of the 1988 Constitution. One can observe that in 1978, there was no progressiveness; that is to say, the lower-income deciles did not receive benefits proportionally higher when compared to 1988. Although there was some backtracking in 1998, there was a strong surge in redistribution in 2008. The increase in access to old-age benefits that are not earnings-related has been fundamental for raising redistribution via social security.

The reduction in poverty after the payment of benefits is more robust and effective in 2010, after the consolidation of the 1988 Constitution, which set a floor for the minimum wage, and facilitated access to benefits for rural workers, the aged, and families with incomes below a quarter of the minimum wage. According to Tafner (2006), families with elderly persons have income levels 43 per cent above those that do not.

In short, the 1988 Constitution expanded benefit coverage for those with few regular contributions, linking benefits to the minimum wage floor that came fully into effect in 1991, and increased family income associated with old-age benefits as well as increasing the number of families covered. The improved financial status and reduction in poverty among the oldest cohorts and the poor is striking, as intended by the design of these policies.

Table 1. Social security transfers as a percentage of Brazilian family income according to family income deciles

<table>
<thead>
<tr>
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<tbody>
<tr>
<td>1</td>
<td>7.3</td>
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<td>29.1</td>
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<td>2</td>
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<td>14.6</td>
<td>38.0</td>
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<tr>
<td>3</td>
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<td>11.5</td>
<td>18.7</td>
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<td>16.4</td>
<td>38.8</td>
<td>43.9</td>
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<tr>
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<td>8.1</td>
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<td>12.2</td>
<td>23.1</td>
<td>23.5</td>
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<td>6</td>
<td>9.3</td>
<td>9.6</td>
<td>21.2</td>
<td>23.9</td>
<td>24.0</td>
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<tr>
<td>7</td>
<td>7.5</td>
<td>9.2</td>
<td>14.0</td>
<td>20.9</td>
<td>20.3</td>
</tr>
<tr>
<td>8</td>
<td>7.8</td>
<td>9.0</td>
<td>15.2</td>
<td>19.4</td>
<td>18.6</td>
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<tr>
<td>9</td>
<td>8.1</td>
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<td>15.5</td>
<td>18.7</td>
<td>17.0</td>
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<tr>
<td>10</td>
<td>8.0</td>
<td>9.4</td>
<td>15.5</td>
<td>17.4</td>
<td>15.3</td>
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<tr>
<td>Total</td>
<td>8.1</td>
<td>9.5</td>
<td>15.6</td>
<td>20.5</td>
<td>20.0</td>
</tr>
</tbody>
</table>

Source: PNAD microdata for selected years.
Effectiveness of public policy: Controversy over inequality

Payment of old-age benefits raised income protection coverage for the oldest cohorts to patterns comparable to countries of Western Europe. Beyond that, it also generated an impact on household income, serving to reduce poverty (Matijascic and Kay, 2013).

One of the principal criticisms of public policy has been the level at which the minimum wage is set, and to which pension benefits are linked. As noted by Tafner (2006), a point of contention is that pension income for poor households serves as an important source of family income, and therefore is a disincentive to accepting low-wage employment, thereby distorting the labour market and making the country less competitive. The Bolsa Família programme has received similar criticism, albeit that Giambiagi and Tafner (2007, p. 167) have argued that Bolsa Família is less distortionary than the minimum wage.

However, that argument does not take into consideration studies, such as those summarized in Figures 2 and 3, which utilize the poverty line in Brazil. A later study by Giambiagi and Tafner (2010) also does not mention empirical studies of inequality. This approach differs from other studies, which focused on the impact of benefit payments (IPEA, 2010, p. 10).

With the new legal framework after the 1988 Constitution, the payment of old-age benefits reduced vulnerability in the older population with respect to access to income. Figures 2 and 3 show the results for families in extreme poverty, i.e. income below one quarter of the minimum wage per capita, before and after the payment of old-age benefits in 1988 (before the 1988 Constitution had an impact) and in 2012.

Inequality is also an ongoing concern in Brazil. The 30-year movement of the impact of old-age pensions on reducing inequality can be seen using the Gini coefficient, which was 2.6 per cent in 1978, 3.3 per cent in 1988, 5.5 per cent in 1998, and 10.3 per cent in 2008. This is noteworthy given that improvements were limited prior to the 1988 Constitution, with progress accelerating after its implementation. Significantly, inequality decreased more substantially between

2. Giambiagi and Tafner (2007, 2010) also argue that the burden of Brazilian civil servants’ pension schemes is not relevant to measure the impact on public finances. Nevertheless, data for 2004 presented by Palacios and Whitehouse (2006) show that Brazil spent about 4.8 per cent of the GDP on civil servants’ pensions and was ranked first when compared to non-OECD countries, where the average was 1.3 per cent. Tunisia, Zimbabwe, and Turkey – the countries ranked second through fourth – spent about 2.5 per cent of GDP. In OECD countries, the average spent on civil service pensions was about 1.9 per cent, with the top two countries, Austria and Belgium, with expenditures of about 3.7 per cent of GDP. The new pension scheme for Brazilian public servants put in place in February 2013, creating pension funds for workers with incomes above the national ceiling, will take decades before they contribute to a reduction in the fiscal burden.
Figures 2 and 3. Poverty as a percentage of the cohort before and after paying pension in 1988 and 2012

Source: PNAD microdata for selected years.

1998 and 2008, especially after the purchasing power of the minimum wage increased in 2004.

Initiatives like IPEA (2010) are not sufficient to provide a comparative international benchmark. Using the Gini coefficient, or reductions in inequalities, provides a clearer indicator when comparisons are made with other countries.

Esping-Andersen and Myles (2008) demonstrate that the welfare states of Western Europe and North America achieved reductions in inequalities that are more or less pronounced regarding the level of decommodification of each country with respect to social protection. In other words, the less the redistribution of income or access to social services depends on the market, the greater the potential reduction in inequality. Furthermore, based on Marical et al. (2006), the authors find that greater potential for reducing inequalities comes from the provision of social services, which accounts for why the Nordic countries achieve greater equality.

In applying the criteria of Marical et al. to Brazil, the reduction in inequality after income transfers or social services\(^3\) was higher than that of the Nordic countries. Thus, social policy in Brazil was positive in terms of the reduction in inequalities through social services or income transfers, respectively, as measured by the Gini coefficient. Brazil’s results were better than other welfare state-typologies according to Esping-Andersen and Myles (2008),\(^4\) in contrast to Giambiagi and Tafner (2007, 2010). The comparative results for reductions in inequalities via the provision of social services and income transfers were:

- Universal or Social Democrat typology: 37 per cent (social services) and 16 per cent (income transfers)
- Liberal typology: 24 per cent (social services) and 4 per cent (income transfers);
- Conservative typology: 24 per cent (social services) and 3 per cent (income transfers), and,
- Brazil (data for 2008): 41.5 per cent (social services) and 18.5 per cent (income transfers).

Figure 4 demonstrates the impact of different social policies on inequality following Marical et al. (2006) and shows that health and education have an

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3. The social services described here included health and education, which were the only sectors analyzed across the member States of the Organisation for Economic Co-operation and Development (OECD). Not using policies targeted at specific segments of the population hides the impact of the improvement in well-being in societies that use these types of services. It is important to note that France, and above all the Nordic countries, have a wide range of social services recognized as being highly effective.

4. Esping-Andersen (1990) analyzed welfare states from Western Europe, Oceania, and North America. After calculating the degree of decommodification related to labour market dependency, Esping-Andersen concluded that the results presented three different models: Social Democratic, Conservative and Liberal. The Social Democratic model was characterized by a low level of dependence from the labour market and an extensive menu of non-contributory universal social services. The Conservative model relied on income protection and was targeted to workers belonging to dominant social professional groups, with a minor role for social services. Finally, the Liberal model relied basically on market provision and social protection is focused on those who cannot find regular jobs.
especially powerful impact on income distribution and reductions in inequality. It is important to note that income transfers have statistical composition effects and aggregate data cannot simply be composed from its constituent parts.

Matijascic and Kay’s (2010) results presented in Figure 4 have limits. None of the countries that are compared to Brazil has similar per capita income levels or labour market structures with such ineffective regulation and such large informal sectors. It would be useful to compare and benchmark Brazil to neighbouring countries with similar per capita income levels. Brazil’s high scores presented in Figure 4 are potentially misleading. Given that Brazilian income distribution is so regressive, not least because labour market regulation and tax policy does little to reduce income inequality, social policies can therefore potentially achieve major outcomes regardless of their efficacy and efficiency.

These results have important implications for public policy. The finding that social services, especially health care, have a bigger impact on reducing inequality is significant. That is to say, in a country with such high inequality, there are limits to what can be achieved by income transfers via old-age pensions, whereas expending additional resources, on education and health care especially, can be more effective in reducing inequality.

The consolidation of the social protection model focusing on offering support to families, but in a context where private institutions cater to those with higher incomes, is still dominant in Brazilian social policy. While the 1988 Constitution represents progress toward the goal of universal coverage and the Social

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**Figure 4. Per cent share of inequality reduction after transfers according to the Gini Index in 2008**

<table>
<thead>
<tr>
<th>Total Social</th>
<th>31.8</th>
</tr>
</thead>
<tbody>
<tr>
<td>Education and Health</td>
<td>27.6</td>
</tr>
<tr>
<td>Health care</td>
<td>19.1</td>
</tr>
<tr>
<td>Education</td>
<td>13.1</td>
</tr>
<tr>
<td>All cash transfers</td>
<td>13.1</td>
</tr>
<tr>
<td>All pension</td>
<td>11.0</td>
</tr>
<tr>
<td>Old age and Disability</td>
<td>8.8</td>
</tr>
<tr>
<td>Survivor pension</td>
<td>3.5</td>
</tr>
<tr>
<td>Unemployment insurance</td>
<td>1.1</td>
</tr>
<tr>
<td>Bolsa Familia</td>
<td>0.6</td>
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</tbody>
</table>

Democratic model, the persistent deficiencies in the quality of public social services means that Brazil cannot be labelled a “welfare state”.

A possible counter-argument is that the lower levels of per capita income in Brazil and limited infrastructure are obstacles to forming a welfare state. The level of quality of health and education services, especially compared to other countries with similar per capita income levels as Brazil, is poor.

The quality of services provided through the social protection system presents challenges, especially with respect to health care and education. Matijascic and Kay (2013) showed that coverage for health care was very unequal, especially in the poorest regions or poorest metropolitan neighbourhoods. Inadequate access to coverage and assistance for health care reduces healthy life expectancy in Brazil, as defined by the World Health Organization (WHO, 2009), and results are poor when compared to neighbouring or the other BRICS countries (Russian Federation, India, People’s Republic of China and South Africa). Although Brazilian healthy life expectancy is higher than in countries such as Bolivia, India, South Africa or the Russian Federation according to 2007 data, the total years of non-healthy life is higher in Brazil. This data suggests that disease prevention is insufficient, with the Unified Health System (Sistema Único de Saúde – SUS) prioritizing curative treatment before prevention.

Moreover, Brazil’s history of privileging cash transfers over social services is clearly at the crossroads. Public opinion polls show that dissatisfaction with health care and education is the most significant. According to the WHO (Estadão, 2013), public spending on health care is below the world average. This problem is particularly acute given that more than 70 per cent of the population cannot afford to pay for private health care. This lack of investment, along with ineffective budget expenditures, reflects years of lost healthy life that contributes to higher spending on curative medicine (which leads to higher costs than would be the case with investment made in effective preventive care). Last, but not least, the loss of healthy life may accelerate pension system expenditures and lower labour productivity. These social policy challenges have a direct impact on economic performance.

The distribution of funds between cash transfers to families and social services is overly biased towards cash benefits, which is problematic if the aim is to reduce inequalities and promote social cohesion. If we consider pension benefits,

5. Quality is also a concern with educational policies, as Brazil’s scores in the Program for International Student Assessment (PISA) are very poor, even when compared to countries with lower per capita income. Only 3.8 per cent of Brazilian students achieved a score 4 or higher in mathematics, or, conversely, more than 95 per cent of students aged 15 did not meet expected levels of performance. Performance in language and the sciences are also poor. Among South American countries, only Colombia and Peru received lower scores in mathematics, although Brazil’s financial resources and state capacities are higher than those of most of its neighbouring countries (OECD, 2010).
conditional cash transfers and unemployment insurance, Brazilian spending is equivalent to 17.1 per cent of GDP. Health care expenditures are equivalent to 3.6 per cent of GDP, much lower than the 4.1 per cent of GDP spent on private health plans. An additional 5.9 per cent of GDP was spent on education (2011). The share destined for social services such as education and health care is low given that more than 70 per cent of families depend on public health care exclusively, and about 86 per cent of families depend upon public education.

Conversely, spending on survivor benefits is equivalent to 3.2 per cent of GDP, a share that is much higher than in other countries (James, 2009). According to data from the ILO6 and OECD,7 total spending on survivor pensions in Chile is about 1.9 per cent of GDP, compared to 1.3 per cent in Argentina and 0.3 per cent in Mexico. In OECD countries, the average is about 0.9 per cent of GDP (with Italy spending 2.5 per cent of GDP and Belgium spending 2.1 per cent of GDP). Given that the importance of the male breadwinner model has declined, expenses for survivor benefits should decrease and in a few decades become marginal. If, hypothetically, Brazil’s survivor benefit expenditures as a percentage of GDP were equivalent to those of Italy or Belgium, countries with a male breadwinner tradition and demographically-older populations, it could raise expenditures by 31 per cent (63 per cent when compared to the OECD median). In short, the fiscal impact of survivor benefit policies should not be underestimated.

It is important that the singular features of Brazil’s social security system are fully considered – to do otherwise leads to analytical errors. Giambiagi and Tafner (2010) and Schwarzer and Santana (2013) present analyses based on labour markets characterized by stable salaried employment. This is not, nor has it ever been, the case in Brazil, as described above, where over 80 per cent of benefits paid to workers in the private sector were unfinanced or partially financed by contributions. These studies utilize examples that compare the collection of contributions as a percentage of salaries and benefit expenditures. This is problematic given that little over one third of Brazil’s economically active population contributes while 95 per cent of the population aged 70 or older has access to benefits. To exclusively tax workers who make contributions to social security would result in exorbitant contributions or would result in restricted access or severe benefit cuts.

Article 202 of the Brazilian Constitution obliges the government to provide funds to pay social security expenditures and, if needed, introduce specific taxes to finance social security or to raise tax rates. Giambiagi and Tafner (2007, 2010)

and Schwarzer and Santana (2013), among other experts, do not take this into consideration, and instead present calculations based on INSS or public service pension schemes’ collections and expenditures. This omits value added taxes and taxes on profits, both of which are required by the Constitution to fund the social security budget. As a result, calculations based on constitutional mandates result in major surpluses rather than deficits. Omitting these other sources of revenue can be misleading, since policies that may be cost effective can still show deficits depending on how they are accounted for in the budget (Matijasic and Kay, 2008).

How Brazil’s demographic profile is accounted for is also important. Giambiagi and Tafner (2010) and Schwarzer and Santana (2013) warn that Brazil is ageing rapidly and without constitutional reforms, the system will become unviable given the tight relationship between contributors and beneficiaries. However, in a society with disproportionately few contributors yet nearly universal coverage, this will require, as we have seen, the transfer of fiscal resources. Furthermore, the ratio of contributors to beneficiaries can be modified by:

- Reducing informality in the labour force, which will increase social security contributions as has been the case in Brazil over the past decade; and/or
- Improving health conditions and epidemiological monitoring to reduce disability benefit rolls as well as health care expenditures.

In considering dependency ratios, age is only one consideration, and developing effective policy requires taking a broader perspective on the labour market.8

Living conditions remain precarious, given that the inequality of income in Brazil is still amongst the highest in the world and more than 46 per cent of the population live in houses with poor sanitation (IBGE, 2012). In other words, cash transfer policies are important, but they have limits, since their main objective is to transfer income between generations and not social groups. Social services, economic, social and environmental regulation, as well as taxation and public policy expenditure, have a major role to play, indeed a more prominent one if the goal is to reduce inequality and promote higher levels of development.

8. If we analyze the employment-adjusted dependency ratio – which incorporates those leaving work temporarily due to illness, disability or unemployment, or being economically inactive – the proportion of dependant workers expands dramatically. For example, in comparing Brazil with two industrialized countries for which data is available, we get a sense of how dependency expands. In France and Spain, the population aged 65 or older compared to the population aged 15 to 64 in 1990 and 2003 was: 21.3 per cent and 24.8 per cent in France, and 20.7 per cent and 24.8 per cent in Spain (Whiteford, 2005). However if the employment-adjusted dependency ratio is used, the results for those same years were 102.4 per cent and 101.6 per cent in France, and 133 per cent and 105.6 per cent in Spain. For Brazil, using the same methodology for the years 1990, 2003, and 2012, the results would be 108.9 per cent, 102.4 per cent, and 84.3 per cent. This demonstrates how considering employment conditions is vital for developing effective public policies.
The neglected role of institutional and administrative reforms

Since the passage of the 1988 Constitution, there has been an ongoing debate over the need for market-friendly reforms that promote private investment and financial stability by reducing the tax burden. Giambiagi and Tafner (2010) advocate constitutional reform to achieve these objectives, arguing that rural and public assistance pensions have perverse effects, more so even than the distortions created by the pension schemes for public-sector employees.

The political Left in Brazil defends these benefits with ideological zeal, considering these legal protections to be untouchable. Fagnani (2011) and Cohn (2010) emphasize the reduction in inequalities, and defend without distinction the universal benefit floor and statutes that protect the aged and rural retired workers, and other less equity-enhancing rules concerning survivor benefits, the accumulation of multiple benefits, and rules allowing workers to receive benefits while still being employed.

None of these arguments advocate adopting major parametric reforms, most of which do not require constitutional amendments. Parametric reforms can be targeted at benefit plans and management practices, not to mention the adoption of benchmarking according to international standards as discussed by Gillion et al. (2000), or, most recently for minimum social security guarantees, by the International Labour Organization’s Recommendation concerning national floors of social protection, 2012 (No. 202).

Most financially-effective reforms would not exclusively depend upon constitutional reform. It is important to note that reforming ordinary legislation or changing administrative practices can have fast, powerful, and long-lasting effects to reduce income inequality and promote social cohesion.9

One difficulty is the current nature of the debate in Brazil. Stakeholders commonly adhere to their own epistemic universe, ignoring other arguments. A more sober perspective suggests that the Constitution, on the one hand, privileges

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9. Constitutional reforms involving pension benefits are required for legislation on minimum and maximum benefits, minimum age, years of contribution and different types of benefit (such as old-age, survivor, sickness, maternity, unemployment, etc.). Specific eligibility criteria such as accumulating wages and benefits or qualifying for survivor benefits only require ordinary legislative reforms. Furthermore, rules about disability are legislated by the Federal Administration using decrees within the INSS. This is not to say that the issue does not involve very sensitive political problems. In 1997, President Cardoso issued a Decree that prohibited receiving pensions while being employed. At the time as the constitutional reform was under consideration in the Senate, President Cardoso came under intense pressure to revoke the Executive Decree (Matijasic, 2003), which he did in order to restart negotiations (Amendments 19 and 20, were approved in December 1998). This demonstrates that even a measure that did not require a constitutional reform – a rule prohibiting collecting a pension while being employed – can face intense opposition from vested interests (and how the judiciary would have responded will never be known).
universalism and, on the other hand, protects corporative interests, especially among State employees and philanthropic institutions. Until February 2013, State employees were not subject to the same pension ceiling as private-sector workers. Philanthropic institutions are immune to taxation, including payroll taxes as employers, and are not monitored on a regular basis to evaluate their performance and accountability. Put bluntly, the Constitution did not create mechanisms to prevent the transfer of income to the better-off and sustains mechanisms that stimulate income concentration and a regressive tax model.

The possibility of accumulating benefits and pensions or old-age benefits along with earned income was described in detail by Matijascic and Kay (2008, 2013). We argue that there is no justification for:

- Paying full and not partial benefits if a person works full time. Starting with Bismarck’s legislation, pensions have been meant to replace income after one can no longer work;
- Providing lifetime survivor benefits to those not in a position of economic dependency. Survivor benefits are intended for spouses that do not enter the labour market, school-age orphans, or the disabled;
- Accumulating multiple retirement pensions and survivor pensions while also receiving income from full-time work. Such a situation is not a social right and diverts public resources from more productive uses;
- Allowing premature retirement, which is not a social right and unduly burdens public finances.

According to Figure 5, over 25 per cent of pensioners work in full-time jobs, as is the case for more than 20 per cent of those older than age 65, accumulating both sources of income. From 1978 until 2012 the situation has not substantially changed. Nevertheless, among those aged 65 or older, there is a smaller contingent of pensioners that remain in the labour market in 2012. This situation probably means that increments of income for lower deciles stimulate the elderly to effectively retire when they are entitled to pensions.

If a person works full time, it does not make sense for them to receive a full retirement pension benefit. It is essential to emphasize that in Brazil there is no part-time regular old-age pension to facilitate a gradual exit from the labour force.

Most Brazilian social policy experts do not criticize the possibility of accumulating benefits while working full-time. On the contrary, what is commonly argued is that benefit levels are too low and that returning to work is necessary (Follador, 2013). However, the average old-age retirement pension benefit amounted to 64.4 per cent of average earnings for workers aged 16–64 contributing to social security in 2012, while for those that work and receive retirement pension benefits and survivor pension benefits it represented 96.3 per cent of average earnings. Moreover, according to the Brazilian National Household Sample Survey (PNAD, 1978–2012) data in 2012, for those who earned retirement pension benefits and
received a regular salary, the figures were equivalent to a 106.2 per cent replace-
ment rate and for those accumulating retirement pension, survivor pension ben-
efits, and regular income from work the figure was equivalent to 180.8 per cent. It
is clear that those who are better off can accumulate different sources of income,
which concentrates income distribution.

The persistence of these rules, which have existed since the 1930s, is a clear
demonstration that legislation needs to be understood in light of prevailing pat-
terns and practices. It is precisely those receiving higher benefits, with higher
replacement rates, that return to the labour force. In contrast, there are severe
restrictions in accessing benefits for those workers with a more precarious link to
the labour market. These restrictions include:

• The requirement to contribute for 15 years and reach age 65 for men and age 60
for women to be eligible to receive a retirement pension in an urban area. These
are strict requirements when compared to other countries (Table 2);
• Individuals who become unemployed and cease contributing lose their
insurance and give up their right to benefits in the event of disability or death (sur-
vivors), even if they have contributed for a lengthy period;
• Access to non-contributory benefits is contingent on family per capita earnings
up to one quarter of the minimum wage, which necessitates means-testing.

Matijascic and Kay (2010) show that if the poverty line were measured accord-
ing to OECD methods (i.e. half of workers’ median earnings), poverty in Brazil

Figure 5. Per cent share of employed pension system contributors receiving lifetime
pensions (figures includes all types of pensions)
would be reduced by only 2 per cent, and not more than 30 per cent. Thus, the arbitrary value given to the poverty line is a determinant of the success or failure of policy.

In presenting the options for those with access to stable employment along with the options for those with fewer opportunities, there is little doubt: the financial impact of legislation concerning benefits in Brazil favours the better off, who received higher earnings from more stable occupations. Table 2 lists the legislation of a range of countries. The minimum requirements for receiving a pension benefit in Brazil is among the strictest, because it requires a contribution period of 15 years, while in other countries it may only require affiliation or residency or shorter periods of contribution.

Administrative comparisons are difficult without benchmarking, nevertheless, it can be observed that:

- The large number of social security institutions is inefficient. Without monitoring the health status and capacity to work of beneficiaries, the risk of fraud increases (incidents of fraud are regularly reported in the media);
- There are a large number of personnel devoted to administrative work and comparatively few working in areas that directly serve the public. This helps to explain negative views of public services; and,

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**Table 2. Entitlement requirements and minimum age for old-age pensions eligibility**

<table>
<thead>
<tr>
<th>Country</th>
<th>Minimum contributions (does not include social assistance benefits)</th>
<th>Minimum contribution (for full pension)</th>
<th>Age (male/female)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brazil</td>
<td>15 years of contribution</td>
<td>35/30 years of contribution</td>
<td>65/60</td>
</tr>
<tr>
<td>Russia</td>
<td>5 years of coverage</td>
<td>No requirements</td>
<td>60/55</td>
</tr>
<tr>
<td>India</td>
<td>10 years of coverage</td>
<td>No requirements</td>
<td>55</td>
</tr>
<tr>
<td>China</td>
<td>15 years of coverage</td>
<td>Actuarial through contribution</td>
<td>60/50–60</td>
</tr>
<tr>
<td>Chile</td>
<td>10 years of contribution</td>
<td>20 years of contribution</td>
<td>65/60</td>
</tr>
<tr>
<td>Mexico</td>
<td>25 years of contribution</td>
<td>25 years of contribution</td>
<td>65</td>
</tr>
<tr>
<td>Portugal</td>
<td>15 years of contribution</td>
<td>30 years of contribution</td>
<td>65</td>
</tr>
<tr>
<td>Italy</td>
<td>5 years of contribution</td>
<td>42 years of contribution</td>
<td>66</td>
</tr>
<tr>
<td>Germany</td>
<td>5 years of contribution</td>
<td>35 years of coverage</td>
<td>65</td>
</tr>
<tr>
<td>Sweden</td>
<td>3 years of contribution</td>
<td>No requirements</td>
<td>65</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>1 year of contribution</td>
<td>30 years of contribution</td>
<td>65/61</td>
</tr>
<tr>
<td>United States</td>
<td>No requirements</td>
<td>No requirements</td>
<td>66</td>
</tr>
</tbody>
</table>

Much needs to be done with respect to organization and methods. Services are slow, public works are continuously delayed, and State purchasing is slow due to very ineffective legislation.

Reform of the State is an urgent priority, and reforming social security will be a key component. For example, Brazil spends more than 3 per cent of total benefits spending on administrative costs, while the United States and Switzerland spend 0.7 per cent and 0.4 per cent, respectively (Matijasic and Kay, 2008).

Institutional or managerial changes can free up resources for other priorities, including raising benefit levels or improving public social service infrastructure in the interior of Brazil, where health services are more limited and the quality of service is often precarious. This translates into fewer years of healthy living and disproportionately high levels of ill health, as described by Matijasic and Kay (2008). Clearly, a new development strategy is needed to reduce income concentration and create job opportunities for the population. Social services can obviously be used as leverage to improve social development. Moreover, relevant pension reforms do not require constitutional amendments and can be achieved by means of ordinary legislation or administrative decisions.

Policy proposals: Towards a pension model adapted to the labour market

Brazil’s pension system plainly has room for improvement. To base a pension system on payroll taxes in a low-wage economy with a low density of contributions and high levels of informal employment (with high levels of self-employment and domestic service work) is problematic. In turn, permitting the accumulation of benefits for those who remain employed serves to concentrate income and limits capacity to adopt policies to promote employment, especially youth employment. Permissive survivorship pensions represent a further misallocation of resources.

The pension system could achieve effective rates of coverage and improved equity with a first-pillar universal benefit, a second-pillar contributory benefit based on earnings, and a third voluntary pillar regulated by the State. As regards the first pillar, this would be a single non-contributory universal benefit for those who were no longer able to work, offering a means to achieve universal coverage with low administrative costs. Coverage would be made available to all who satisfied the age condition or who were assessed as disabled and incapable of work, so that if a person ceased contributing because they could no longer work, they would still have access to benefits, as is the case in many other countries. A contributory second-pillar benefit would permit income smoothing for those with higher earnings.

For those who do contribute regularly there could be easier access to credit from financial institutions, linked to total contributions. Firms, as well as...
individuals, would have access, and this would provide incentives for firms to follow best governance and disclosure practices. Pensioners may get easier and significantly cheaper access to credit if the periodic repayments for loans are deducted directly from their benefit payments. Additional credit measures could be considered for those who regularly contribute, as a way of recognizing that their income risk is far lower than for those who are not contributing regularly.

A simpler tax code would end the confusing and efficient practice of multiple taxes; Federal agencies and social security taxes frequently overlap. A fewer number of taxes and simpler rules would lead to greater efficiency. The diverse range of administrative authorities and tax rolls is inefficient and raises costs. A single registry would lead to administrative efficiencies and help prevent the current high levels of fraud. The monitoring and cross-checking of administrative records could free up a significant amount of resources.

The absence of a reserve fund makes the retirement system vulnerable to short-term financial conditions. A reserve fund is called for in the Constitution and should be implemented – it can also help smooth the demographic transition as the population ages. The decentralized units of government which manage benefits can also be used as a tool to audit and detect potential fraud. There should be incentives for local administrative units to benefit from recovered contributions or the cessation of benefits due to irregularities. Professional organizations, trade unions, and civil society movements may also support this effort by participating in campaigns to promote the importance of paying contributions.

The accumulation of benefits and salaries should be considered from a legal perspective. Benefits were designed to substitute for wages when a worker was no longer able to earn income. The possibility of accumulating salaries and benefits impedes policies to encourage or postpone retirement with the aim of improving labour market conditions.

Pension policies affect both social rights and public finance, and remain an intensive source of debate. Policy legacies from decades past continue to elevate costs while the failure to adhere to principles enumerated in the Constitution means that measures to reduce inequality and promote social cohesion are not undertaken.

Conclusions: What has changed and what has not?

The principal challenges facing Brazil’s pension system stems from the fact that it combines social insurance with social assistance where coverage is nearly universal for the aged, but contributions are made by a limited segment of the working-age population. Under such circumstances, it is impossible to achieve financial equilibrium between contributions and benefits. The social security budget, which utilizes fiscal resources to fund benefits, is somewhat regressive, but addresses these
conditions. Yet current rules permit the accumulation of multiple benefits and the granting of survivorship benefits that are extremely generous. These represent significant policy challenges that must be included as part of any administrative and institutional reforms.

Brazil’s recent social policy achievements stem from the 1988 constitutional reform, which was the result of a broadly participatory process that impeded the adoption of structural reforms that might have left the elderly population more vulnerable. Yet, the reluctance to reduce generous contributory benefit entitlements that are a legacy from the past is an obstacle to more equity enhancing reforms.

Furthermore, the much discussed recent reduction in income concentration via cash transfer benefits and tax incentives cannot stimulate further progress in income distribution without more investment in economic and social infrastructure, and, perhaps even more so, better social services to assist a rapidly ageing population with relatively low education levels and poor health conditions.

In other words, to defend the status quo without acknowledging the need to improve both efficiency and equity is disingenuous, while it is also a mistake to adopt models from other countries that do not take into account the specific dimensions of Brazil’s labour market (with its significant informal sector) as well as other economic, social, and demographic factors. As a precondition for reform, the range of distributional consequences of the current system, which contains both progressive and highly regressive features, must be systematically described and fully considered.

Social policies that are better adapted to social conditions – and the ending of pension entitlements that have nothing to do with social rights and which may contribute to the deterioration of social cohesion – are essential. Such reforms are necessary to modernize the State and improve labour relations in order to consolidate a new equity-improving development path.

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The Brazilian pension model: The pending agenda


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Social protection assessment-based national dialogue exercises: Cambodia, Indonesia, Thailand, Viet Nam

Valérie Schmitt and Rachael Chadwick

International Labour Organization, Regional Office for Asia and the Pacific, Bangkok, Thailand

Abstract Between 2011 and 2013, the International Labour Organization, in collaboration with governments and several United Nations agencies working as part of the Social Protection Floor Initiative, conducted social protection assessment-based national dialogue (ABND) exercises in Cambodia, Indonesia, Thailand and Viet Nam. The exercises were carried out in order to take stock of existing social protection realities in the respective countries, including social insurance, social assistance and anti-poverty programmes. These inventories present a comprehensive picture of what elements of national social protection floors (SPFs) are in place, where “holes” in national floors exist, and provide a framework within which to propose recommendations for the further design and implementation of social protection provisions that guarantee at least the SPF to the entire population. This article describes the methodology for conducting ABND exercises, the situational analysis of the SPF in four countries, and the policy recommendations that were formulated for achieving basic health care and income security for children, the working-age

Addresses for correspondence: Valérie Schmitt (schmittv@ilo.org) and Rachael Chadwick (rachael.chadwick@gmail.com), International Labour Organization, Regional Office for Asia and the Pacific, United Nations Building, Rajdamnern Nok Avenue, P.O. Box 2-349, Bangkok 10200, Thailand. The article builds upon considerations raised by the 2013 special double issue of the International Social Security Review to provide evidence with regard to challenges and opportunities for the implementation of national floors of social protection (SPF). The authors wish to acknowledge the authors of the SPF assessment reports upon which this article is based; namely, Michael Cichon, Florence Bonnet, Carlos Galian, Gintare Mazeikaite, Jean-Claude Hennicot, Wolfgang Scholz, Sinta Satriana, Dr Thaworn Sakunphanit, Orawan Prasitsiriphol, and the many others who contributed to the compilation and production of each respective report.
population and the elderly. The results of preliminary calculations of the cost of implementing proposed policy options are also outlined.

**Keywords** social protection, social security, Cambodia, Indonesia, Thailand, Viet Nam, South East Asia

**Introduction**

Between 2011 and 2013, the International Labour Organization (ILO), in collaboration with governments and several United Nations (UN) agencies working as part of the Social Protection Floor Initiative, conducted several social protection assessment-based national dialogue (ABND) exercises in East and South-East Asia. The exercises took stock of existing social protection realities in order to understand what elements of national social protection floors (SPFs) were in place, where “holes” in national floors exist, and to propose recommendations for the further design and implementation of social protection provisions that would guarantee at least the SPF to the entire population.

This article describes the methodology for conducting ABND exercises. The methodology was developed by the ILO in the Asia and the Pacific region and tested in Cambodia, Indonesia, Thailand and Viet Nam. The article includes an overview of the four completed ABND exercises and the resulting recommendations for achieving basic health care and income security for children, the working-age population and the elderly, to provide a situational analysis of the SPF in each country. The results of preliminary calculations of the cost of implementing proposed policy options are also outlined.

While socio-political and economic contexts vary between and within Cambodia, Indonesia, Thailand and Viet Nam, ILO experts observed key parallels in the challenges to – and opportunities for – securing basic health care and income security for children, the working-age population and the elderly. These findings have relevance not only for social protection and development agendas globally, but also illustrate how the SPF framework is a useful tool for policy-making, programme planning, analysis of poverty, and as an approach that incorporates the needs of vulnerable groups.

1. The ABND exercises were supported by the ILO-Korea partnership programme, Government of the Netherlands, Government of Finland, UN Office for South-South Cooperation, Grand Duchy of Luxembourg, and ILO-European Union project.
2. For Cambodia, see Hennicot and Scholz (2012) and Hennicot (2012); for Indonesia, see Satriana and Schmitt (2012); for Thailand, see Schmitt, Sakunphanit and Prasitsiriphol (2013); and for Viet Nam, see Bonnet et al. (2012).
What is the SPF and what is its relevance to poverty?

What are social protection floors?

Social protection floors are nationally-defined sets of basic social security guarantees that aim to prevent or alleviate poverty, vulnerability and social exclusion (see ILO, 2013a). By calling for both demand (transfers) and supply side (services) measures, the SPF adopts a holistic approach to social protection. SPFs, as defined in the ILO’s Recommendation concerning national floors of social protection, 2012 (No. 202) (ILO, 2012a), encompass social protection and social security, both as rights and policy choices, establishing that rather than delineating two distinct notions they are “actually part of the same social policy concept” (Hagemejer and McKinnon, 2013, p. 9).

Countries are encouraged to prioritize the implementation of SPFs as a fundamental element of their national social security systems and as a starting point for the provision of higher levels of protection to as many people as possible, as soon as possible, in line with economic and fiscal capacity.

SPFs should comprise, as a minimum, the following nationally-defined sets of goods and services or basic social security guarantees:

a) access to essential health care, including maternity care, at a nationally defined minimum level that meets the criteria of availability, accessibility, acceptability, and quality;

b) basic income security for children at a nationally defined minimum level, including access to nutrition, education, care, and any other necessary goods and services;

c) basic income security at a nationally defined minimum level for persons of active age who are unable to earn sufficient income, in particular in the case of sickness, unemployment, maternity, and disability; and

d) basic income security at a nationally defined minimum level for older persons.

Defining the components of SPFs as “guarantees” establishes a degree of flexibility that makes the achievement of the floor compatible with all possible national social protection systems. The four guarantees set minimum performance or outcome standards with respect to access to, scope, and level of income security and health care, rather than prescribing a specific architecture of social protection systems, programmes, and benefits.

While not all countries will be able to put all components in place for their entire populations immediately, the SPF provides a framework for planning the progressive implementation of holistic social protection systems that emphasize linkages and symbiotic relationships between the different SPF guarantees.
Social protection floors and the international context

The ILO has developed, over a number of decades, a comprehensive set of internationally-accepted standards in relation to the establishment, development and maintenance of national social security systems. These standards, however, have not proved suitable in all country contexts, especially where a large proportion of the workforce is engaged in the informal or rural economy. The international community has come to recognize that there is a need for new standards and approaches that could guide countries on how to close coverage gaps, and this has paved the way for increased utilization of the SPF approach at the international level.

Perhaps most relevantly, the International Labour Conference adopted the Recommendation concerning national floors of social protection 2012 (No. 202) at its 101st session in 2012. Recommendation No. 202 reaffirms the role of social security as a human right and as a social and economic necessity, and provides guidance to countries in building SPFs within progressively comprehensive social security systems.

Social protection floors in the Asia and the Pacific region

While the Asia and the Pacific region has made considerable economic progress in the last two decades and has lifted millions out of poverty, not all have benefitted from these gains. Millions of people are still poor, deprived of basic rights, and vulnerable to increased risks stemming from global economic crises and climate change (World Bank, 2013). The threat that human development gains made in the past decade may fail to “stick” and begin to reverse has helped to place social protection high on the policy agenda in the region.

At their 67th session in May 2011, member States of the UN Economic and Social Commission for Asia and the Pacific passed a Resolution on strengthening social protection systems in Asia and the Pacific (UN ESCAP, 2011). At the ILO’s 15th Asia and the Pacific Regional Meeting held in December 2011 in Kyoto, Japan,

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5. See ILO (2012a). The ILC also adopted a Resolution concerning efforts to make national floors of social protection a reality worldwide, which invites governments, employers and workers to jointly give full attention to implementing Recommendation No. 202 as soon as national circumstances permit. See ILC (2012).
6. On 29 February, 2012, the World Bank announced that the developing world had met the first Millennium Development Goal – namely, to reduce extreme poverty (as measured by the population living under USD 1.25 a day) by half. Poverty-reduction efforts in East and South East Asia, led by the People’s Republic of China and Indonesia, played a key role in this achievement. See World Bank (2012).
The assessment-based national dialogue: ABND methodology and results

A multidimensional conceptualization of social security is necessary to establish a clear view of where gaps in coverage lie. Hagemejer and McKinnon note how “On the basis of the more precise identification of coverage gaps, policy planning to remedy such gaps can be facilitated, policy implementation improved and policy outcomes made more effective” (Hagemejer and McKinnon, 2013, p. 5). In recognition of this, the ILO collaborated with governments, social partners, civil society, academics and several UN agencies in East and South-East Asia in 2011–2013 to conduct social protection assessment-based national dialogue exercises in Cambodia, Indonesia, Thailand and Viet Nam.

The studies utilized similar methodology, with the common objective of assessing whether the SPF is a reality in the respective countries. Policy gaps and implementation issues were identified and recommendations were made for the further design and implementation of social protection provisions that would guarantee a SPF for the entire population. The studies also sought to estimate the projected financial commitment needed in each country to implement proposed policies for closing “holes” in the SPF. As part of the social protection assessments, in each country the ILO Rapid Assessment Protocol (RAP) costing tool was used to estimate the cost and affordability of implementing social protection recommendations.

Social protection realities in Cambodia, Indonesia, Thailand, and Viet Nam

The social protection situation in each of the four countries assessed is of course unique to their respective socio-economic contexts. However, some revelatory

7. The RAP uses a simple methodology that builds on single age population projections and single age estimates of labour force participation rates, along with a relatively crude economic scenario determined by assumptions about overall GDP growth, productivity, inflation, wages, interest and poverty rates. The model uses these variables as drivers of expenditure and revenues starting from initial statistical values given for the last observation years.
Similarities and differences between countries were identified when considered within the framework of the four guarantees of the SPF.

The governments of Cambodia, Indonesia, Thailand and Viet Nam all allocate a large share of their social protection expenditure for health care, for example – between 40 and 70 per cent of total public social protection expenditure (Figure 1).8 Thailand and Viet Nam – which both have old-age pension schemes for formal-sector workers – spend between 37 and 49 per cent of total social protection public expenditure on income security for older persons, whereas public spending on income security for the elderly is much lower in Indonesia and close to zero in Cambodia. Indonesia is already investing a significant share of its public social protection expenditure in children (23 per cent), yet this SPF guarantee is underdeveloped in other countries. Social protection for the working-age population is relatively underdeveloped in all countries.

The ABND methodology

The ABND approach assists countries to identify and address “holes” in their social security system in order to move towards the achievement of a nationally-defined SPF. Following the adoption of Recommendation No. 202, it remains for individual countries to carry out national consultations grounded in social dialogue and social participation, to use these avenues to create policy space and new social

8. ILO Social Protection Department database (update in April 2013).
security policies, and to thus create the political will required to free fiscal space (Hagemejer, and McKinnon, 2013). Cognizant of this requirement, the ABND methodology employs a participatory approach to identifying priority policy options for the successful and coordinated development of nationally-defined SPFs. All relevant stakeholders including line ministries, local government bodies, workers’ and employers’ organizations, civil society organizations, academia, and development partners, are involved from the onset.

ABND exercises involve three main steps: (1) building an assessment matrix, (2) the rapid assessment protocol, and (3) finalization and endorsement of an ABND report.

**Step 1: Building the assessment matrix**

The assessment matrix lists and describes existing social security schemes for each of the four SPF guarantees, identifies policy gaps and implementation issues, and provides policy recommendations for the further design and implementation of social protection provisions, with the aim of guaranteeing (at a minimum) the SPF to the entire population (Figure 2).

The completed assessment matrix answers the following questions:

- What is the social security situation in the country for each of the four SPF guarantees (access to health care and income security for children, income security for the working-age population, and income security for the elderly)?

9. For the purposes of this article, “fiscal space” uses Heller’s (2005) definition: “the availability of budgetary room that allows a government to provide resources for a desired purpose without any prejudice to the sustainability of a government’s financial position”. In cases where budgetary capacity is not sufficient, the government may create additional fiscal space by raising corporate income tax, value added tax or personal income tax, borrowing from international institutions or markets, or cutting down on low priority expenses. However, borrowing beyond a certain extent has to be carefully considered, as it may compromise macroeconomic sustainability in the long term.
For each guarantee, what are the different schemes? What are the planned schemes? For each scheme, what segments/percentages of the population are covered? What are the types of transfers (cash, in-kind, access to services)? What are the levels of benefits? Do legislative provisions (or a lack thereof) exclude some segments of the population from social protection and/or social security schemes (are there policy gaps)? Are some parts of the population excluded in practice (implementation issues related to inclusion/exclusion errors, budgetary constraints or mismanagement)? What can be recommended to close policy gaps and solve implementation issues?

To build on the results of the assessment matrix, workshops involving all relevant stakeholders are organized, in addition to bilateral consultations.

**Table 1. Main recommendations to complete the SPF for health care**

<table>
<thead>
<tr>
<th>Recommendations</th>
<th>Cambodia</th>
<th>Indonesia</th>
<th>Thailand</th>
<th>Vietnam</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extend existing social health protection schemes</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>to greater segments of the population or introduce</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>universal health insurance</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase levels of benefits of existing schemes</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Improve supply-side measures</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
</tbody>
</table>

- For each guarantee, what are the different schemes? What are the planned schemes?
- For each scheme, what segments/percentages of the population are covered? What are the types of transfers (cash, in-kind, access to services)? What are the levels of benefits?
- Do legislative provisions (or a lack thereof) exclude some segments of the population from social protection and/or social security schemes (are there policy gaps)?
- Are some parts of the population excluded in practice (implementation issues related to inclusion/exclusion errors, budgetary constraints or mismanagement)?
- What can be recommended to close policy gaps and solve implementation issues?

Assessment matrices in Cambodia, Indonesia, Thailand, and Viet Nam. Assessments of the social protection situations in each country were carried out using the ABND matrix format, listing and describing existing provisions and policy and implementation gaps, and using them to formulate recommendations against each of the four SPF guarantees.

- Health (Table 1). The ABND exercise in Cambodia found that high out-of-pocket health expenditures were the cause of impoverishment, indebtedness and the forced sale of livelihood assets for the poor and near-poor. Cambodia’s National Social Protection Strategy for the Poor and Vulnerable promotes the extension of health protection for the poor and vulnerable through the expansion of health equity funds and community-based health insurance schemes. In line with this objective, the central policy option proposed for extending social health protection was the extension of health equity funds to all very poor and poor persons.

10. This section summarizes some of the key findings from the ABND exercises carried out in the four countries. For the full assessment matrices and findings, please see the full ABND reports as referenced in footnote 2.
Indonesia committed to achieving universal health insurance coverage under the 2004 National Social Security System Law and 2011 Social Security Providers Law. The ABND exercise highlighted that until this system is rolled out, around 41 per cent of the population remain uncovered by health insurance. Accordingly, the recommendations put forward relate to the form and level of benefits under the new system (e.g. inclusion of some treatments for diseases currently excluded from existing schemes, such as preventive and curative treatments for HIV), and the extension of benefits to progressively larger segments of the population.

Viet Nam’s 2008 Law on Health Insurance came into effect on 1 July 2009, with the aim of achieving universal health insurance by 2014. The ABND exercise did not identify any policy gaps in the Government’s strategy for achieving universal coverage; however it questioned the feasibility of extending health care coverage to the 40 per cent of the population presently not covered – which mainly comprises informal-economy workers – through voluntary insurance. Proposals to address implementation gaps included investments on the supply side in terms of staffing, equipment and consumables, and increased subsidies for a large proportion of the uncovered population.

While Thailand is the only country of the four to have achieved universal health coverage, the ABND exercise nevertheless identified challenges such as an unequal distribution of health care facilities between rural and urban areas, quality of care issues in rural areas, and lack of coverage for undocumented migrant workers. Furthermore, the laws and institutions governing the health insurance system are fragmented, with some legislative conflicts. While no recommendations were made for additional social protection provisions in relation to health, the Thai ABND report did propose structural reforms and improved operations to establish a unified and financially sustainable health insurance system.

- **Children.** While the range of existing social protection programmes targeting children varied across the four countries, the ABND exercises identified similar policy and implementation gaps, such as limited programme coverage, supply-side issues such as quality of education, and problems with data management and beneficiary targeting. In all countries, the introduction of (or expansion of existing) cash transfer programmes were proposed as a means of achieving income security for children, reducing school dropout rates and fighting against child labour (Table 2).

- **Working-age population** (Table 3). Provisions for the working-age population tabled and described during the ABND exercises in Cambodia, Indonesia, Thailand, and Viet Nam span a variety of schemes and programmes ranging from...
social security funds for veterans,12 public-sector workers and private-sector employees, to public works,13 vocational training and employment creation programmes. Key parallels in policy and implementation gaps among the country case studies and between different schemes were observed. Social assistance and welfare programmes, for example, were found to often receive insufficient budget allocation and suffer from limited effectiveness and ad-hoc distribution. Challenges to the extension of social security to larger segments of the population, particularly to informal-sector workers, were also noted in all countries.

Recommendations for achieving income security for the working-age population in each country primarily related to the extension of existing, or introduction of new, social security benefits, and improving linkages between employment creation programmes and social security schemes. In Indonesia, Cambodia and Viet Nam the establishment of public works guarantees linked with vocational training were proposed, while in Thailand a combined benefit package comprising income

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12. The definition of “veterans” varies among the four countries. In Cambodia, for example, veterans are persons certified as war veterans, and former civil servants and laymen who enrolled as soldiers during the war.

13. There is no single accepted definition of what constitutes a public works programme. For the purposes of this article and the ILO’s approach, the following definition is appropriate: “Public works programmes (PWP) refer to the more common and traditional [public employment] programmes; although these may be a temporary response to specific shocks and crises, public works programmes can also have a longer-term horizon. Cash and food for work programmes are included in this term”. (Lieuw-Kie-Song and Philip, 2010, p. 3).
support measures and mechanisms to increase employability and/or access to markets were suggested.

Each of the ABND exercises also identified shortcomings in social protection coverage for disabled people under existing schemes targeting the working-age population. To address these deficiencies, additional measures were proposed. In Thailand for example, an increase of the Universal Non-Contributory Allowance for People with Disabilities was recommended; likewise in Indonesia, where the extension of the existing non-contributory pension scheme to all people with severe disabilities was suggested. In Cambodia and Viet Nam, where disability is a major issue (affecting 1.4 per cent and 3.7 per cent of the respective populations), recommendations included a means-tested pension for the disabled in Cambodia, and the inclusion of social assistance for those unable to work in Viet Nam’s proposed employment guarantee scheme.

The ABND recommendations in Cambodia and Thailand also included the introduction of maternity benefits in the form of cash transfers to poor women who are pregnant (in Cambodia) and to women working in the informal economy who have just given birth (in Thailand). The ABND exercise in Thailand additionally recommends the introduction of a sickness benefit to compensate for loss of income for hospitalized Thai informal-economy workers.

• Elderly. A finding common to all ABND matrix results was that an insufficient proportion of the elderly population was covered by old-age benefits. Where they do exist, benefits are largely limited to private-sector and public-service employees and are insufficient to ensure income security. In Viet Nam for example, a compulsory pension insurance scheme covers approximately 18 per cent of the workforce; other targeted social assistance programmes provide benefits for elderly persons aged 80 years or older, and poor elderly aged 60 years or older, who have no relatives to rely on. The majority of informal-sector workers have no protection in old age. Those elderly who are entitled to social pensions receive benefits that are below both the rural and urban poverty lines.

Recommendations stemming from the four ABND exercises accordingly focused on increasing benefit levels of, and access to, old-age pensions. Additionally the establishment of a long-term care system was recommended in Thailand (Table 4).

From Step 1 to Step 2

The recommendations stemming from the ABND exercises fall into one of two categories. The first type of recommendations relates to the expansion of the SPF, and proposes to:

• cover more people;
• increase levels of benefits of existing non-contributory schemes;
introduce new non-contributory benefits or programmes.

The cost of implementing such recommendations can be assessed using the ILO RAP model.

The second category of recommendations may propose:
• new or expanded mandatory or voluntary social insurance (e.g. “establish an unemployment insurance system”);
• initiatives related to the operation of and coordination between schemes (e.g. “improve targeting mechanisms”);
• qualitative measures (e.g. “improve the education system”).

For the second kind of recommendations, the cost of implementation requires in-depth studies that are beyond the scope of an ABND exercise. The ILO rapid assessment protocol (RAP) model is, however, suitable for assessing the cost of introducing the first type of recommendations. To facilitate the cost calculation process, broad policy recommendations were translated into specific policy options or scenarios.

**Step 2: Rapid assessment protocol (RAP) model**

Fulfilment of the four guarantees or rights that comprise the SPF require foundational social protection programmes that are long-term, fundamentally non-contributory and funded through public resources or the government budget. Financing must be predictable and secure over the long term (Harris, 2013). In recognition of the need to consider both how initial efforts will be financed and how to sustain these efforts over time, ABNDs include a costing exercise that determines the available and necessary fiscal space for introducing SPFs. After transforming broad policy recommendations into specific policy options or scenarios, the costs of proposed social protection provisions were estimated and forecast over a ten-year period using the ILO RAP model (Figure 3). This costing exercise aims to provide an evidentiary basis for discussions on available fiscal space and government budget re-allocations, in turn helping with the prioritization of possible social protection policy options.

The ILO RAP model is an Excel tool including three types of sheets:

### Table 4. Main recommendations to complete the SPF for the elderly

<table>
<thead>
<tr>
<th>Recommendations</th>
<th>Cambodia</th>
<th>Indonesia</th>
<th>Thailand</th>
<th>Vietnam</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extend existing pension schemes to greater segments of the population or introduce a universal social pension</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Increase benefit levels of existing old age allowance, or index benefits on inflation or poverty line</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Introduce a long-term care system</td>
<td></td>
<td></td>
<td></td>
<td>✓</td>
</tr>
</tbody>
</table>
· **Type 1.** A variety of data is entered under the themes: general government operations, labour market, demographic and macroeconomic data.14

· **Type 2.** Each policy option proposed based on the ABND matrix results is described in detail, with a choice of parameters. Data from the Type 1 sheets is used to calculate the cost of introducing the policy options.

· **Type 3.** In these sheets the final results of the RAP model are presented. In each of the four countries, a number of combined SPF benefit packages were proposed, including a choice between “low” and “high” cost packages, thus providing governments with a range of options. The results of the cost calculations and projections were expressed in national currency, as a percentage of GDP and as a percentage of government expenditure.

*Applying the RAP tool in Cambodia, Indonesia, Thailand, and Viet Nam*

For each of the ABND recommendations that were translated into policy options/scenarios in each respective country, the RAP tool was used to calculate the cost of

14. A range of data was entered, including population data per single age and sex, together with population projections; male and female labour participation rates per age group; data on the economically active population; various economic indicators such as inflation rate, minimum wage, poverty line and GDP growth (used to calculate the cost of social protection provisions and to express the cost as a percentage of GDP); and information on the government budget (used to express the cost estimates of proposed policy options as a percentage of government expenditure).
implementing the proposals as stand-alone initiatives, as well as part of consolidated packages to close the SPF. The country reports offer a full description of the policy options and scenarios proposed (see footnote 2).

Cambodia. In Cambodia, individual policy proposals were calculated, on the basis of which a low and a high combined benefit package were proposed (Figure 4). Based on these two combinations, the cost of a complete SPF package for Cambodia was projected at between 0.4 per cent and 2.4 per cent of GDP by 2020. While performing the cost estimation exercise in Cambodia, the main assumptions included a high GDP growth rate and a rapid decline in the poverty headcount. Figure 4 shows that the cost of implementing the scenarios decreases over time.

Indonesia. For the Indonesian costing exercise, a low and a high scenario of combined benefits was proposed (Figure 5). Based on these two combinations, the cost of completing the SPF in Indonesia was calculated to be between 0.74 per cent and 2.45 per cent of GDP by 2020.

15. For the full list of policy options costed and details of calculations/combined benefit scenarios, see Hennicot (2012, pp. 13–27).
16. For the full list of policy options costed and details of calculations/combined benefit scenarios, see Satriana and Schmitt (2012, pp. 59–73).
Thailand. As in the Indonesian and Cambodian ABND costing exercises, both a high and a low scenario for combined proposed schemes were considered in Thailand (Figure 6). Based on the two package options, completing the SPF in Thailand would cost an estimated 0.50 to 1.21 per cent of GDP by 2020.

Viet Nam. In Viet Nam, costing exercises were carried out for four different social protection packages, each comprising different combinations of proposed benefits. Based on the two package options, closing the SPF gap in Viet Nam would cost an estimated 1.98 and 6.06 per cent of GDP by 2020 (Figure 7).

Affordability and fiscal space

The ABND exercises additionally included some preliminary analysis of the affordability of the proposed recommendations for the respective countries. Affordability is assessed by calculating the cost of the new social protection schemes and comparing this cost with GDP. If the estimated cost of implementing a proposed social protection scenario is low – 1 per cent of GDP for instance – it may be argued that the country in question can afford to extend the additional social protection benefits.

17. For the full list of policy options costed and details of calculations/combined benefit scenarios, see Schmitt, Sakunphanit and Prasitsiriphol (2013, pp. 52–70).

18. For the full list of policy options costed and details of calculations/combined benefit scenarios, see Bonnet et al. (2012, pp. 25–31).
Figure 6. Thailand: Cost estimate of low and high combined benefit packages (percentage of GDP)*

* Though the graph is relatively simple, it illustrates where Thailand sits in relation to establishing a comprehensive social protection system. The country has already achieved the social protection floor for health care, for example (universal health insurance); consequently, none of the policy options presented in the graph are related to health care.


Figure 7. Viet Nam: Cost estimate of low and high combined benefit packages (percentage of GDP)

Source: Bonnet et al. (2012).
Depending on policy choices and the social model of the country, these additional expenditures may be:

- fully financed through social contributions (made by workers and employers);
- or
- fully or partially financed from the government budget. In such cases it is important to assess whether the government can afford these additional expenditures, i.e. whether there is sufficient fiscal space.

One of the recommendations included in the assessment report for Viet Nam, for example, is to gradually increase personal income tax to about 1.3 per cent of GDP and increase value added tax by about 1 percentage point, which might be sufficient to generate the 2.3 per cent of GDP estimated to be required for closing the SPF financing gap, while keeping the overall government deficit at a projected level of 3 per cent of GDP.

**Step 3: Finalization and endorsement of the ABND reports**

Proposals for the freeing of additional fiscal space to make room for new policy initiatives typically comprise a relatively small percentage of a country’s overall budget. However such new initiatives must compete with existing policy priorities. Political and consequent budgetary commitments are thus necessary for resources to be committed to/made available for social protection (Harris, 2013).

In recognition of this, the ABND exercises first provided recommendations on completing the social protection floor and costing estimates using the RAP model (as outlined above), and then shared the proposals with government representatives, workers, employers, and civil society organizations with a view to technically validating the report and receiving political endorsement.

The technical validation process can be lengthy and time consuming, given the number of actors involved, particularly the number of relevant ministries: health, education, labour, social affairs, planning, finance and so on. In Thailand, a national coordination mechanism was helpful in speeding up the process. The National Commission on Social Welfare Service Promotion – which includes representatives of all relevant line ministries – coordinated and compiled all technical comments on the draft report.

The endorsement process may involve:

- organizing bilateral meetings with high-level policy-makers to explain the recommendations and seek their support;

19. Technical validation includes the confirmation of the description of the social security situation (the assessment matrix), endorsement of the proposed scenarios, and validation of the parameters and assumptions used in the cost calculations.
inviting high-level policy-makers to write an acknowledgement of the report;
organizing a high-level launch event for the report with press coverage;
developing a number of tools (videos, leaflets) to explain the main recommendations of the report;
involving civil society networks and workers’ and employers’ representatives to advocate for some of the recommendations.

In Thailand, for example, the ILO presented the report to the Minister of Labour, Minister of Social Development and Human Security, Secretary General of the National Economic and Social Development Board (NESDB), the Prime Minister’s Office and relevant permanent secretaries. The ILO secured their participation in the report launch and they agreed to write an acknowledgement for the report. The report was launched at Government House by the Minister attached to the Office of the Prime Minister, together with the Minister of Labour and the Minister of Social Development and Human Security. More than 300 participants representing the Royal Thai Government, Thai workers’ and employers’ organizations, civil society, academia, embassies and international organizations attended the event. This major event lent high visibility to the ILO’s work in Thailand, and paved the way for future collaboration between the UN Country Team in Thailand and the Royal Thai Government in further supporting the recommendations of the ABND report.

A similar process was carried out in Indonesia, where the ILO presented the final report to the Vice Minister of the State Ministry of National Planning Development (Bappenas) and gained support from Bappenas for a joint launch of the assessment report on 6 December 2012.

Implementing the SPF: Challenges and opportunities

While the preliminary assessments and calculations set out above demonstrate that progressive establishment of a nationally-defined SPF is possible and affordable, implementation faces a number of challenges in each of the four countries and in the Asia and the Pacific region more broadly. ILO Recommendation No. 202 includes a number of guiding principles that, if applied in national contexts, will help overcome these implementation challenges.

Coherence and coordination

A lack of coherence across policies was observed in each of the ABND exercises, with multiple and sometimes contradictory legal frameworks compounded by limited collaboration and communication between line ministries and social security institutions. In Thailand for instance, the co-existence of a number of different old-age pension schemes contributes to inefficiencies, administrative
burdens, and protection risks from the lack of portability of benefits across schemes.

National consensus

Achieving coherence with social, economic and employment policies across the institutions responsible for delivering social protection is among the guiding principles of Recommendation No. 202 (ILO, 2012a). The ABND exercises can support efforts to attain coherence at the policy level by building a national consensus on social protection priorities and the extension of social protection. Such a consensus can form the foundation of national social protection strategies. In Cambodia for example, the RAP model contributed to the development of the National Social Protection Strategy. The ABNDs that are planned or underway in Lao People’s Democratic Republic, Mongolia and Myanmar will be instrumental in developing the national social protection strategies of these countries.

Coordinating mechanisms

The establishment of coordinating mechanisms is critical to ensure that coherence is sustained at the policy and implementation levels in the long term. It is difficult for a single line ministry (i.e. a ministry of health or social welfare) to achieve effective policy coordination, as their respective mandates do not embrace all dimensions of the SPF. Successful coordination mechanisms can be established, however, at a supra-ministerial level. In Thailand, the National Commission on Social Welfare Service Promotion is a platform for coordinating all social welfare policies, chaired by the Prime Minister. In Indonesia the National Social Security Council is responsible for coordinating the implementation of the new social security laws. In Cambodia a special Social Protection Coordination Unit was created under the Council of Agriculture and Rural Development.

At the implementation level, effective coordination can be established by using common targeting mechanisms to identify beneficiaries. In Indonesia, the National Team for the Acceleration of Poverty Reduction has developed an integrated targeting mechanism and a consolidated database for all poor households. Similarly, the Identification of Poor Households programme in Cambodia has established a common targeting mechanism which is used by several social assistance programmes.

At the subnational level, coordination between programmes can be improved through common social protection delivery mechanisms, where people can be informed, registered, and directed to adapted social protection programmes. Similarly, information on programme coverage and utilization of services can be collected and updated. This can also be instrumental to increasing the capacity of
local governments to deliver social services, to respond to the needs of local populations, and to establish efficient complaints and appeals mechanisms. This kind of coordinating service is currently being developed in Cambodia (called the Social Service Delivery Mechanism) (Schmitt, et al., 2013) and piloted in Indonesia (called the Single Window Service).

Adequacy and predictability of benefits

Lack of resources and/or insufficient financing, resulting in the poor availability and quality of public social services and low levels of benefits, is a significant challenge to achieving social protection for all in Asia and the Pacific. In Cambodia, for example, the monthly survivors’ pension for veterans does not cover the cost of two meals.

In countries such as Cambodia, some programmes are still donor-funded. Many programmes are not yet embedded in national law, as is the case with the old-age minimum pension scheme in Thailand. As a consequence the existence, level of benefits and qualifying criteria for accessing benefits are subject to change from one year to another, depending on donor budget allocations or government policy.

The ABND exercises undertaken in the four countries demonstrate that investing in higher levels of basic social protection is not only necessary but can be affordable and sustainable in the long term.20

Universal coverage

Many of the existing social protection programmes in countries in Asia and the Pacific are underpinned by the idea that only poor households should be exempted from paying contributions, and that other groups of the population (which inevitably includes vulnerable groups and informal-sector workers), should contribute at least in proportion to their capacity to pay. As a consequence, significant numbers of informal-sector workers are excluded from most or all social protection schemes. They are not poor enough to receive social assistance or welfare benefits, but are not legally covered by social insurance, or when they are, not willing to contribute to social security schemes with benefit packages that do not meet their needs, payment schedules that are incompatible with their (often irregular) income flows, and contribution levels they perceive as too high.

20. This is in line with the guiding principles of ILO Recommendation No. 202, according to which benefits should be adequate and predictable, and financial, fiscal and economic sustainability should be achieved with due regard to social justice and equity (ILO, 2012a).
To implement targeted social transfers, sophisticated and costly vulnerability assessment tools and poverty databases must be established. Targeting methods based on proxy means testing inevitably lead to inclusion and exclusion errors. This is the case with the ID-Poor database in Cambodia and the Team for the Acceleration of Poverty Reduction database in Indonesia.\(^{21}\)

Although the results of the ABND studies in Indonesia, Cambodia, Thailand, and Viet Nam demonstrate that universal schemes are affordable in all four countries, many policy-makers remain to be convinced. In spite of Thailand’s ten years of experience with a universal health care scheme, policy-makers in the country do not agree with UN SPF team’s recommendation that a universal child support grant be established and are instead considering child grants targeting poor children only. Such policy orientations make achieving “universality of protection, based on social solidarity” (ILO 2012a) – the first guiding principle of Recommendation No. 202 – a more challenging prospect in the medium term.

### Management information systems

Insufficient development of national registry databases and beneficiary identification systems makes the task of reaching out to potential recipients and expanding social protection coverage particularly difficult. When national registration systems are in place, however, the ease of extending non-contributory benefits is greatly improved. It is estimated that in countries such as Thailand – where all nationals have a 13-digit identification card – introducing new, targeted benefits (such as maternity benefits for all pregnant female workers in the informal sector) would only take two to three years.

Despite attempts to harmonize targeting procedures and tools (for instance via the ID-Poor database in Cambodia and the similar targeting mechanism established in Indonesia), none of the four countries studied has yet achieved a comprehensive and integrated management information and monitoring system, and information remains scattered across line ministries and social security programmes. This limits opportunities for exchanges of information and thus the potential to update data, and makes it difficult to monitor the overall extension of coverage.

In Cambodia for example, the management information system designed for the Social Service Delivery Mechanism will include a list of final beneficiaries, a list of all programmes, and information on how beneficiaries can access the

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21. The information feeding these databases is only updated once every three years. As a significant share of the population move in and out of poverty relatively frequently, the data defining who is poor and who is not is often inaccurate. In Indonesia, for example, TNP2K data indicates that approximately 53 per cent of those defined as poor in 2008 had moved out of poverty in 2009, while 22.3 per cent of those who were near-poor in 2008 became poor in 2009.
programmes. This will provide the information necessary for monitoring the
delivery of services and coverage of beneficiaries and will also be instrumental in
evaluating the impact of social protection provisions on graduation out of poverty.

Recommendation No. 202 advocates for “tripartite participation with represen-
tative organizations of employers and workers, as well as consultation with other
relevant and representative organizations of persons concerned” (ILO, 2012a).
However, unlike social insurance schemes that are often governed by tripartite
boards, the beneficiaries of social assistance or welfare programmes are in many
cases not consulted during the design phase, and not represented in the decision-
making bodies of these schemes. Innovative mechanisms to ensure proper repre-
sentation need to be designed and established. In Cambodia participation will be
ensured by involving elected commune councils in the supervision of the Social
Service Delivery Mechanism, as well as various committees representing the inter-
est of the population. Workers’ and employers’ representatives who were so far
excluded from these committees will also be included during the implementation
stage. In addition, a complaint and appeals mechanism will enable the receipt of
feedback from, and dialogue with, all relevant parties.

Information on, and understanding of, entitlements

Without appropriate information on existing social protection programmes and
entitlements to social security guarantees, significant segments of a country’s
population may lack the knowledge and access needed to participate in, and
benefit from, existing forms of protection. The role of civil society in countries
such as Thailand has been a key determinant in creating awareness and advocating
for policy changes in the field of social protection. In countries where access to
information is limited, education tools and campaigns need to be designed and
implemented from the sub-district level up. This includes education tools that
target specific groups, such as children; the development of information brochures
and other educational products for dissemination; public service announce-
ments;22 and broadcast media such as radio dramas. All these measures may con-
tribute to increased understanding of entitlements to benefits.

Conclusion

The ABND exercises carried out in Cambodia, Indonesia, Thailand and Viet Nam
produced useful baseline surveys of the social protection situation in each country,
in turn enabling identification of policy and implementation gaps in line with the
four guarantees of the social protection floor, as set out in the Social Protection

22. For an example of public service announcements, see ILO (2013b).
Floors Recommendation, 2012. The assessment matrices informed the development of both policy proposals and costing models for implementing measures to close social protection floor gaps in each country.

While these products – the ABND matrix, list of policy gaps and implementation issues, policy recommendations, costing exercises and fiscal space analyses – are important and useful within each country for governments and other stakeholders as they pursue national social protection priorities and policy planning, the ABND model has broader relevance for other countries seeking to improve their social protection environments.

The use of a national dialogue with representatives from government, non-government, workers’ and employers’ organizations to produce the ABND matrix allows the social protection situation to be captured from a range of perspectives and enables progressive consensus-building on key social protection ideas in line with the four SPF guarantees. This facilitates a holistic definition of a national SPF that aligns with the visions of different segments of society – and thus will vary from one country to another. This lends legitimacy to domestic policy choices, helping to secure the necessary fiscal space and in turn helping to ensure their sustainability.

The ABND approach, combined with the RAP costing tool, additionally acknowledges that any policy options proposed to close the social protection gaps identified must be translated into policy scenarios that the country can afford, while allowing flexibility for schemes to be progressively scaled up as greater fiscal space becomes available. As such, the ABND model is suitable for, and adaptable to, a range of country contexts both within and beyond the South-East and East Asia region.

The ILO is continuing to promote the ABND approach and methodology through:
- the provision of technical and policy guidance to stakeholders involving similar social protection assessment exercises in other countries;
- the development of a Social protection assessment based national dialogue: A good practices guide (see Schmitt and De, 2013) to be used as a training resource for policy-makers and to inform the conduct of social protection assessments at country level;
- the organization of hands-on training workshops on the SPF at country and regional levels.

The guide will be part of a global effort by the ILO to develop good practice guides on social security – one of the key goals of the ILO’s Social Security for All strategy (ILO, 2012b).

These efforts will contribute to the development of a comprehensive knowledge base on the social protection situation in Asia and the Pacific and to further promote the development of national SPF.
To translate the recommendations of the ABND reports into concrete SPF implementation, a number of challenges need to be overcome, as highlighted in the final section of this article. The ILO’s Recommendation concerning national floors of social protection, 2012 (No. 202) prescribes a number of guiding principles that, if applied in national contexts, can help to overcome these implementation challenges.

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This is an interesting book for a number of reasons. First, because it covers from a broad social and political perspective the emergence and development of the Spanish welfare state in the context of four decades of multiple transitions – from a totalitarian regime to democracy, from a low-income, mainly rural economy at the periphery of Europe, to a middle-income rapidly modernizing and growing economy, sailing through business downturns, becoming a member of the European Union (EU) and the Eurozone, but having to cope, since 2007, with the mortgage bubble, a banking meltdown, a State solvency problem, a threat to its political unity and its social fabric, with dramatically high and rising unemployment, poverty and exclusion. Its welfare state model diverges from the traditional classification of welfare state models, including the so-called Southern (European) Model, while sharing some of their characteristics and ideological and political underpinnings, which the authors clearly discuss.

The book highlights the development and reform process of the welfare state in Spain, pointing to the real achievements as well as to the shortcomings of its various reform episodes, which need to be addressed especially in the aftermath of the financial and economic crisis that started in 2007–2008.

The 17 authors that have contributed to this volume are well-known academics and senior researchers from various Spanish universities and other research institutions. They are all members of the recently constituted national network ESPAnet-Spain (REPS), affiliated to the European Social Policy Analysis Newtork (ESPAnet).

The volume consists of three parts. Following a general introduction, Part I describes the emergence and consolidation of the post-Franco welfare state in Spain between 1975 and 2010, pointing to three distinct processes; namely, the late development of the welfare state, the acceleration of social and economic change and the consolidation of political democracy, which produced a set of relatively contradictory social policies – notably, the universalization of health care and education, a selected but growing privatization of care services, poorly articulated social assistance and a precarious and segmented labour market (chapter 2). The impact of Spain’s accession to the EU in the mid-1980s and how the European social model contributed to the shaping and development of the welfare state and to the employment policy to cope with high unemployment is analysed in chapter 3. The quest for gender equality in policy-making and in the labour market was particularly important in a country characterized by familialism and a patriarchal approach to social protection and female labour market participation, while tolerating gender pay disparities. These led to significant pro-gender equality legislation, helped by the transposition of EU directives. However, gender discrimination continues because of the strongly dualistic labour market that limits the access of women to decent employment, while the “familialistic” welfare state approach leaves women with the main caring responsibility (chapter 4).
Part II looks at the levels of governance of the welfare state, starting with the role of the social partners in policy formulation and reform via collective bargaining and social dialogue. It is noteworthy that political consensus played a crucial role in the development and transformation of the Spanish welfare state (chapter 5). The regional dimension of welfare regimes, with different configurations in the 17 Spanish autonomous regions, with differing levels of development, has implications for multi-level governance, which is assessed in chapter 6. Chapter 7 looks at the changing public-private mix in the provision of health and social services, with the emergence of private and non-profit organizations. Comparing cross-country attitudes towards the welfare state, Chapter 8 finds that Spain has more extensive support for state intervention in welfare areas, but unemployment protection is inadequate, despite the high incidence of unemployment and precarious jobs, even in periods of rapid growth. Also, childcare expenditure and services are inadequate despite the country having the lowest rates of fertility among OECD members.

Part III points to the six key challenges that the Spanish welfare state has to address: i) the minor role of part-time employment, due to the prevalence of temporary jobs (chapter 9); ii) the huge rise in female employment between 1999 and 2007 (by 50 per cent), which requires a substantial readjustment of the welfare model, since women traditionally assume the caring tasks. Awareness of low fertility and rapid population ageing has brought to the fore the conflict between work and family life, but regional and national measures to address this have had limited impact (chapter 10); iii) the rapid and unprecedented rise in immigration and its implications for social welfare in times of crisis (chapter 11); iv) long-term care in the context of rapid demographic ageing, dominated by informal care by female family members (chapter 12); v) poverty, despite its sizable reduction in the past, is a major challenge for the welfare state in the context of the economic crisis. The current system of means-tested benefits has helped to alleviate the worst aspects of economic insecurity, but it has not addressed more moderate forms of poverty. Indeed, after several decades of poverty reduction, the rate of poverty has not fallen since the mid-1990s. Moreover, as a significant proportion of past job growth was based on low-wage jobs, it provided insufficient earnings to avoid poverty. While new schemes were developed to broaden the safety net and benefits were better targeted, the system has not managed to provide complete coverage to all households at risk of poverty. Four measures are needed to improve the means-tested benefits: namely, harmonizing the mosaic of welfare schemes into a universal income guarantee, upgrading benefits to adequacy levels defined by EU standards, coordinating regional programmes providing minimum income benefits to overcome problems of inequality in social entitlements, and designing strategies that improve both economic security and work incentives (chapter 13). The last challenge vi) relates to the long and difficult process of pension reform, which results from all the previous challenges and which is aggravated by the State’s risk of insolvency and the dramatic economic downturn (chapter 14).

The following comments dwell on some of these key challenges.

Unlike many advanced economies where part-time work is important for female labour market entry (voluntary or constrained), it has always been marginal in the formal economy of Spain. The book offers several explanations for this situation. First, the regulatory context, notably the 1980 Spanish Workers’ Statute, limited access to part-time contracts to the unemployed and young people under age 25. This constraint, which was relaxed in 1984, may be attributed to the prevalent approach for full-time life-long jobs for male breadwinners. This was considered as an essential
element of the social order that prevailed in the pre-1975 industrial relations system. Such an approach takes time to change. Second, the regulatory decisions of the 1990s focused on temporary contracts as the single form of flexibility, extensively used by private-sector employers, who resisted part-time work. But even the public sector offered very few opportunities for part-time jobs. Other factors include institutional inertia, conflicting interests of trade unions, government and political parties, and the over-representation of core full-time employees in the collective bargaining process.

The fall in fertility rates and ageing of the population, changes in family organization patterns, the generalized increase in female educational levels and, hence, in employment, generated new needs for public services that should have increased the concern for reconciling work and family life and a more gender balanced welfare system. Apparently, this has not happened. Recent policy changes actually reinforce the traditional male earner-female carer gender division, re-privatizing caring tasks within the family via parental leave and monthly cash benefits for working mothers, while the latest dependency regulation leaves caring responsibility to women, granting priority to concerns of fertility and the ageing population. The authors regret that policy-makers disregarded the possible welfare state options, such as a trade-off between rationalizing public expenditure and increasing women’s employment, or between equity and citizens’ free choice. Nonetheless they note that more egalitarian attitudes towards family roles are taking root: dual earner families are increasingly seen as the preferred model (although only 44 per cent of households are actually dual earners; 43 per cent remain with the traditional male breadwinner model), so a shift in policy orientation may occur.

Turning to immigration, – which started on a large and unprecedented scale in the mid-1990s and rose spectacularly during the period of high economic growth – Spain rapidly became one of the principal destinations for migrants in Europe. In 1998, Spain and Finland were the countries with the lowest proportion of immigrants in the EU-15. A decade later, Spain was the third highest (after Luxembourg and Ireland), with about 5 million immigrants (equivalent to the population of Denmark). This impacted all aspects of employment, housing, education and health care, besides infrastructure. This process took place not through illegal migration, but rather through massive irregular employment without work permits, followed by a significant increase from the mid-1990s in formal employment. Between 2004 and 2008, the pattern gradually shifted. Most migrants became regularized in 2005 (with about 600,000 migrants accessing residence and work permits), in 2006–2007 access to work and residence permits was handled by the employers who contracted with workers in the country of origin, and the range of activities open to work permits was broadened. The enlargement of the EU to Eastern Europe meant an implicit regularization of more than half a million immigrants from 2007 onwards. Spanish economic growth until 2008 cannot be understood without this migrant population who contributed about half of the GDP growth, raised tax revenue and social security contributions that significantly strengthened welfare state sustainability directly, – and indirectly by raising the population activity rate, especially of women (one third of the 12 percentage points increase) –, and by reducing the unemployment rate (by 2 percentage points). And yet, 28 per cent of immigrant non-EU or from enlarged-EU households were below the relative poverty threshold, compared with 18 per cent of the native-born population; and 43 per cent suffered problems of exclusion, compared with 14 per cent among Spaniards or EU-15 households. This shows the limits of the social integration of immigrants in Spain, whose problems were exacerbated by early 2009, when more than 1 in 10 immigrant households were without an income,
about 2.7 times the proportion among Spanish households. In the post-crisis situation, it will be necessary to adapt immigration policy, by focusing more on the qualified population and promoting training for resident immigrants, to re-orient Spain’s growth model towards the knowledge economy. This, however, supposes a structural transformation of the Spanish economy and society. At present it is assumed that at least agro-food, tourism and social care will continue to demand an important volume of labour not available among the current resident population, even if unemployment rates increase. So both qualified and unskilled immigrants will be necessary. Migrant workers will also be necessary to ensure the sustainability of the welfare state, a priority must therefore be given to ensuring their social rights, equality of opportunities and treatment to enhance their social mobility and avoid discrimination.

Last, the pension system’s financial sustainability and adequacy present major concerns that repeated reform attempts over the past two decades have not adequately addressed. The public debate in this area concerns only the mandatory public pension pillar, which was created in the late 1960s as a contributory system (financed by employers and employees). It has expanded gradually to improve both coverage (at present reaching about three-quarters of all workers) and benefit levels. Its financial status has been buoyed by over a decade of economic and employment growth since the mid-1990s, with contributory revenues matching outlays and a reserve fund amounting to close to one year of contributions. But the crisis that started in 2007–2008 is rapidly depleting the reserve fund, as unemployment has hit over a quarter of the active population, including more than half of people below age 25, while a third of those in employment have temporary, low-paid and precarious jobs. The demographic respite due to the small cohorts born during the Spanish civil war (1936–1939) is over, as the pace of new entries to retirement is rapidly and dramatically increasing, implying rising costs that could not be absorbed by the current level of contributions (the number of workers has practically stagnated at about 12 million since 1989). Warnings about sustainability came from various external experts, but all political parties were adamant to preserve and consolidate the existing pay-as-you-go system and the related system of inter-generational solidarity, as well as to aim to converge towards EU social expenditure levels (as a percentage of GDP). This was achieved by a cross-party parliamentary agreement known as the 1995 “Toledo Pact”, which was backed by unions and employers’ organizations. It shifted the pension political debate to the electoral arena.

Despite alerts from the EU in 2003, only modest changes were negotiated with the unions by 2008. But by 2010, the depth of the recession and scale of Spain’s sovereign debt forced the government into negotiating with the social partners a major pension reform that extended the standard retirement age to 67 for eligibility to a full pension with 37 contribution years, restricting access conditions for early retirement, reinforcing incentives for delayed retirement, increasing contribution rates for partial retirement, and extending from 15 to 25 years the period for calculating the pension base. These measures were to be phased in starting in 2013, and were to be accompanied by measures to promote economic and employment growth. Some analysts estimate that this reform will reduce pension outlays by 2 percentage points of GDP in 2027, while the OECD estimate that the reform will significantly improve the long-term sustainability of the pension system, reducing pension expenditure by about 3.5 per cent by 2050, noting that the gross replacement rate will decline by some 7 percentage points (from 81.2 to 74.9 per cent). The authors regret that instead of fostering public debate on the need for reform to ensure the long-term viability of the pensions system, the government limited the discussion to political decision-making and to dialogue.
with the social partners, while the public's and workers' knowledge of their pension rights and contributions remain very limited.

To conclude, the book is a timely contribution to the literature on the welfare reform process and rationale in a rapidly changing economy and society. Of importance, it highlights the role and potential of social dialogue between employers' organizations, trade unions, and the State – sometime bilateral, sometimes tripartite –, which are of particular interest to policy-makers in the current EU recessionary context, with rising sovereign debts, rising and high unemployment, and protests against austerity measures, most of which seek to address the impacts of demographic ageing. Besides, Spain is the fifth largest European economy, whose welfare state seems hitherto not to have been analysed.

Hedva Sarfati  
Independent Consultant  
Geneva, Switzerland
BOOK REVIEW


This book offers an interesting approach to the investigation of social policy, social protection and welfare: the achievement of family well-being across the life-cycle for each individual family member. This takes into account the life-cycle from childhood, through adolescence, adulthood, family formation, parenthood, education, labour market attachment and old age. Almudena Moreno Mínguez, the editor of this volume, notes that while there has been extensive research on changes in family structures and typologies, demographic and economic dynamics, the impact of the gradual entry of women into the labour force and different family policies introduced by various welfare states, sociological and economic research on the family has barely considered family well-being.

This book seeks to fill this gap, with its findings rooted in the context of family change across the family cycle in European countries with different cultural, economic, governance and welfare contexts. This is undertaken by combining different theoretical and methodological approaches to, and on-going research on, the quality of life of individuals who live in families.

The approach adopted is inspired by the concept of equitable and sustainable human “well-being”, developed in recent OECD research, which consists of both individual and social well-being, including such cross-cutting factors as fair distribution and sustainability with regard to available resources and elements that determine quality of life. The book thus considers four perspectives: first, the concept of family well-being as a central concern in economic theory, since individual well-being is partly dependent on the well-being of the family; second, current research results on the well-being of individuals at different stages of the family cycle (i.e. childhood, adolescence, family formation and old age) in the current context of growing risk and uncertainty; third, the impact of immigration and new family dynamics and structures on people’s well-being and quality of life; and, fourth, the gender dimension, notably, the impact of women’s entry into the labour force on the division of labour at home and policies to address the work-life balance.

These concerns are analysed in the volume’s four parts. Part I looks at approaches to conceptualize family well-being, as well as the meaning of concepts such as social quality, and addresses the quality of life of parents with young children in Europe (chapters 2 and 3). Part II is devoted to family, child poverty and well-being in Italy in a European Union (EU) comparative context and the correlation between child well-being and lone parenthood across the OECD (chapters 4 and 5). Part III examines the various aspects of work-family balance and gender, starting with a comparative analysis of parental leave policies, gender equity and family well-being in Europe (chapter 6), new social risks and work-family balance (chapter 7), spousal well-being and the links between household income and parental task division (chapter 8), working parents, family and gender in Spain in an EU comparative context (chapter 9), and evaluating the development of gender, health and welfare in Europe in a historical perspective since 1800 (chapter 10). Part IV is devoted to social work, dealing with youth, the elderly and migrants. It considers the support and
success in youth transitions (chapter 11), public policies to support carers (chapter 12), the well-being of asylum-seeking children in Sweden (chapter 13), and family social work in Spain, seen from the multidimensional approach of empowerment, well-being and the welfare state (chapter 14).

This book brings together no less than 22 academics from different disciplines, mainly sociology, social policy, social work, social welfare, but also social pedagogy, education and economics, from universities in Austria, Denmark, France, Germany, Italy, the Netherlands, Sweden, Spain, the United Kingdom and the United States.

The book contains useful pointers to various factors that can improve policy outcomes for a family’s quality of life, in different social and family contexts, including parents with young children. Discussed here is the role of employment and unemployment in modifying the quality of life for fathers and mothers in 27 European countries. Attention is also given to testing the applicability of the social quality concept to such families across the EU, examining the concepts of relative and absolute poverty among children, exploring the underlying facets related to the nature of labour markets and the complex interactions between joblessness, in-work poverty and the impact of social transfers (i.e. the role of the welfare state). The authors note that the countries that have the most positive outcomes in terms of well-being are those that combine strategies that aim at facilitating access to employment and enabling services (especially childcare) and provide income support. Other topics covered include leave systems, early childhood services and maternal and couples’ employment patterns in 22 countries, which highlight the complex interplay between leave systems, gender and welfare regimes. Obviously, there are different impacts of converging and diverging care leave policies, and of different levels of leave generosity, which have an impact on gender equity and family well-being. Special attention is paid to choices related to reconciling work and family life, looking at how institutional and individual factors determine the risk of spending more time than wished outside of paid work to take care of family members. A specific aspect in this context is the difficulty in determining the division of preferences between work and care among couples with young children. Indeed, it is relatively rare that both spouses agree on their task division preference and that they are able to pursue their preference. Clearly, work-family balance depends also on the family model as much as on individual characteristics such as education, work situation and occupation, national cultural and institutional factors which affect family policies and individual expectations and choices.

A particularly important dimension – given the current labour market situation of young people, notably the high incidence of long-term unemployment, precarious jobs and exclusion (those not in education, employment nor training – NEET) – is the assessment of successful transitions from school to work, from adolescence to adulthood, from unemployment to employment, and moving between precarious jobs. The support to young people from a life course perspective is therefore essential. It is argued that assumptions about success and support for transitions differ according to varying contexts of youth transitions, and should be assessed by analysing factors that underlie individual decision-making and negotiation processes. The authors have tried to enlarge the dominant institutional perspective which reduces success in transitions to work and adulthood to entering the labour market, founding a family and avoiding poverty. They show that assumptions of success and support seen generally as valid actually differ according to different contexts of youth transitions, particularly as regards the increasingly uncertain and precarious labour market. They note that successful transitions include not only stable and well-paid jobs, but also trajectories with which youth can identify. Much more attention should be paid to the actions young people actually
perform, and to analysing their implicit meaning rather than focusing on what young people do not do or do not do enough, or do too early or too late. Differing choices and actions by young people according to socio-economic background, education, gender, ethnicity or labour market structures tend to be interpreted as evidence for the structural determination of their agency through social contexts (for example, the coincidence of early pregnancy with low education, or demotivation for education with low economic status). While in many cases they appear predictable, they are far from absolute. Other factors are at work that can interact in the process of individual decision-making and these should be taken into account as well (e.g. new forms of family and family formation, concepts of work and career beyond existing occupational profiles, changing meaning of what is political and how individual needs and interest connect with collective affairs in the public realm). Structured choices and diversity in realizing meaningful and successful transitions show the potential of young people to mobilize support – informal, from families or peers, and formal, from public institutions – and negotiate their transitions through such interaction.

Another concern is the division of responsibilities between the family and the State in the provision of care for family members. While noting the existence of policies to support carers, which include cash benefits, care leave and in-kind benefits, the authors are concerned that these do not sufficiently meet the challenges that caregivers are faced with, particularly in the widespread informal care system across Europe.

In the final chapter, two authors reflect on their personal experience with family social work and well-being programmes, which they developed and implemented in Spain. They comment on the general methodologies and frameworks used for such work, which they feel are all too often based on stereotypes, reflecting the power structure of society in which the behavioural patterns of families are accepted as natural, leading to passive acceptance that disempowers the families and leads at best to short-term results. The first task of the social worker is to establish a different relational model that enables the individual to reflect and behave differently, and to break free from deeply embedded habits. The authors explain how their approach differed, mainly by involving in a positive manner the family and its individual members in assessing their situation in positive terms, enabling them to define “their” needs and formulate “their” objectives, in other words, helping them to help themselves, by understanding the environment in which they live (including the existing services offered by the welfare state, the role of the community, the school, etc.), defining their key concerns about their children, money, work, housing, etc. This participative process leads family members to develop a forward-looking scenario towards their social inclusion. Such positively formulated diagnostic and assessment proved to be the key to sustainable outcomes once the social workers have completed their intervention. In this process, the social workers must also be dynamically involved as agents of change to help families identify the problems deriving from social exclusion and design programmes to improve their social integration and their family well-being. This experience is obviously relevant to southern European countries where the family remains the most highly-valued institution and the last refuge in the current economic crisis, but should certainly have a broader audience across Europe and beyond, at a time when the welfare state is curtailed and the family is increasingly called upon as the last resort safety net.

Hedva Sarfati
Independent Consultant
Geneva, Switzerland