



Social Policy Highlight

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Dynamic Social Security for Europe: A social model for recovery and growth

A key observation from the recent experience of Europe is that social security reform is increasingly complex. Not only should reform ensure adequate protection for all against covered risks, but it should seek improvements in service quality. And for some benefit programmes, effort is also being put into providing greater choice. The realization of these goals requires giving greater consideration to the input to be offered by those responsible for implementing policy: social security administrations. Consideration must also be given to the roles played by other institutional actors as well as to the influence of overarching factors like globalization, population ageing and the economy. In the current challenging economic context, the European “social model” has shown itself to be necessarily robust but also flexible. However, to better ensure the sustainable delivery of social security programmes and to better support economic recovery and future growth, more adaptation will be required. As this *Social Policy Highlight* concludes, in this regard, it is the responsibility of social security administrations to lead by example.

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Drivers for change

In the region of Europe (here, equivalent to the International Labour Organization’s region of Europe and Central Asia), there are heightened expectations about the institutional nature of, and the need for, social security. Such expectations mean that policy and programme reforms must look beyond the first necessary task of ensuring adequate income protection. Increasingly, reforms must also seek to realize improvements in the quality of benefits and services delivered. For certain benefits programmes, providing beneficiaries with greater choice may also be considered. As a consequence of these ambitious reform objectives, the complexity of the challenges facing social security administrators has increased. These observations form part of the conclusions of an ISSA report: *Dynamic Social Security for Europe*.¹

This issue

- Investigates recent developments and trends in social security in Europe
- Reports on key areas of reform in social security policies and programmes
- Analyses the influence of overarching forces on social security reform
- Discusses the challenges for social security administrators
- Presents key policy messages for the development of social security in Europe

To ensure adequacy and enable the provision of quality and appropriate choices in benefits and services, and to take into account the growing cost of social security, a further conclusion of the report is that all stakeholders have a responsibility to adapt their behaviour. In this regard, recent years have witnessed pension reforms aimed at inducing older workers to defer retirement and to stay in employment longer. Reforms in family benefits now encourage women to both work and have children, and men to share more equally in family caregiving. And recent health-care reforms encourage both providers and patients to rely less on hospital and emergency room treatment and more on prevention and primary care provided in community settings.

Overarching forces in society are also at play in shaping the nature of social security reform in Europe. As specific examples, the report singles out as important the influences of globalization, population ageing, and the social and economic impacts of the crisis.

Key statistics for the region of Europe

- The total population of the Europe region is nearly a billion people, 500 million of whom live in the 27 Member States of the European Union (EU).
- Around 16 per cent of the population is aged 14 or younger.
- Around 22 per cent of the population is aged 60 or older.
- The EU countries spend, on average, close to 27 per cent of GDP on social protection, including health care. In the non-EU countries, social protection spending averages 13 per cent of GDP.
- In the EU countries, social protection is financed predominantly by social contributions (59 per cent) and tax revenues (38 per cent).
- Most Western European countries have achieved near-universal levels of population coverage. In other parts of the region, coverage is lower, often as a result of large sectors of informal work and the chronic underreporting of wages in the formal economy.
- Most countries in the region have well-developed health services. However, some countries have quality gaps and supply shortages, and all of them face financing problems. In the region, health-care expenditures range from over 11 per cent of GDP in France and Switzerland to less than 4 per cent in Kazakhstan.

Globalization

The forces of globalization are placing countries under competitive stress. With capital flowing more freely to those locations that offer the lowest production costs, many governments have come under pressure to relax labour laws, so enterprises can hire and fire workers more easily, reduce employment costs and deploy workers more flexibly. The result of these developments is an increase in temporary and part-time work. In the EU-15, from 1995 to 2006, temporary work increased by 25 per cent, and part-time work now accounts for more than one job in five. Similar developments have occurred in Central and Eastern Europe. These developments heighten the risk of informality and of the underpayment of social contributions.

Generally, for social security systems, globalization poses a risk of declining coverage and benefit adequacy, as governments strive to create business-friendly environments by limiting or reducing social security contribution rates. At the same time, globalization creates a pressing need to assure social security coverage for workers in more precarious jobs. For the EU countries, this complex challenge feeds into developments framed by the concept of flexicurity – the need to promote a combination of flexible labour markets and a high level of social security – and, no less important, into efforts to use employment and social policy to engage actively with the labour market to create not only more but also better jobs. For all countries, the creation of better jobs should also involve the creation of qualitatively better working conditions. Importantly, improvements in indicators of occupational health and safety should also impact positively on measures of general health and well-being and on economic competitiveness and productivity.

Population ageing

Between 1960 and 2000, average life expectancy in the EU increased by four years. In contrast, in the countries of Central and Eastern Europe and the former Soviet Union, there was an important counter-trend in the 1990s, namely, a decrease in life expectancy, mostly among males. However, this trend has since started to reverse itself in most of these countries.

Between 2000 and 2060, average life expectancy in the EU is projected to leap by 8.5 years for men and 6.9 years for women. But fertility rates have fallen well below the required fertility replacement rate of 2.1 births per woman. In the EU countries with highest fertility, France and Ireland, the rates stand at, or just below, 2.0 births per woman. However, the bulk of Europe's countries are at, or below, 1.4. In contrast Tajikistan has a birth rate of 3.3 while Kazakhstan, Kyrgyzstan, Turkmenistan and Uzbekistan have rates of about 2.5.

The European Commission (EC) projects that the combined effect of longer life expectancy and lower birth rates will reduce the ratio of active to inactive persons in the EU from 2.7 to 1 in 2009, to about 1.4 to 1 by 2060. Thus, tomorrow's smaller working population will have to support a greatly expanded inactive population. In the face of this shift and at today's labour productivity rates, current retirement ages, contribution levels and benefit levels cannot all be sustained. Substantial adjustments in social spending will be called for, and indeed are already under way in many countries.

In addition, population ageing will increase the number of persons with chronic health problems requiring long-term care, and increase the cost of such provision. In most countries, health-care costs are rising in response to technical innovation, greater prosperity and demographic ageing. Overall, and despite varied efforts to strengthen pension finance through increasing pensionable ages, better linking benefits to lifetime contributions, and introducing mechanisms to automatically stabilize pension system finances, pension system costs continue to rise.

Because of demographic ageing, the EC³ estimates a need to increase overall social protection expenditure in the EU by 4.7 per cent of GDP by 2060 (see Box 1.). In response, the EU's "Lisbon Strategy" seeks, among other objectives, to deal with the higher fiscal cost of ageing by increasing productivity and raising national employment rates.

The cost of ageing in the EU by 2060, percentage point change in social expenditure/GDP

| Pensions | Health care | Long-term care | Unemployment benefits | Education | Total |
|----------|-------------|----------------|-----------------------|-----------|-------|
| +2.4 | +1.5 | +1.1 | -0.2 | -0.2 | +4.7 |

Source: EC, 2009.
Note: Figures rounded.

As part of this strategic approach, family benefits are being used in the EU, and in non-EU countries, to encourage higher levels of employment among women. More generally, the reform of family benefits seek to better meet the evolving family needs that result from more precarious work and changing family structures. To different degrees, these also seek to address low fertility.

Ultimately, and despite all these different reform approaches, the fiscal costs of population ageing will require social security scheme constituents to pay more for social security and, in some cases, to endure cuts in benefits.

The crisis

The global financial and economic crisis that commenced in mid-2007 has significantly weakened the region's economies. One immediate outcome was a loss in the value of most of Europe's public and private pension funds. These developments have since called attention to other problems associated with private pension systems in particular; namely, weaknesses in governance, high private management fees and the absence of legal specifications for benefit computation.

Despite signs of financial market recovery by mid-2009, public pressure for government action to mitigate the risks of private pensions continues. Governments are responding by providing plan members with clearer information on risks, by developing and improving default options, and seeking improvements in governance and administrative costs. Also, as pension systems in the region become more earnings-related and privatized, the importance of minimum pensions and their possible impact on work incentives are commanding increased attention.

In 2009, the economy of the Euro zone was projected to have contracted by 4.2 per cent; in Central and Eastern Europe, by 3.7 per cent; and in the Commonwealth of Independent States (CIS), by 5.1 per cent.³ While some indicators now suggest that the worst is over, unemployment is still rising and constitutes a serious threat to the region's workforce. For example, unemployment in the EU is projected to reach 10 per cent in 2010.

In this context, Western Europe's comprehensive social security systems, and not least unemployment benefits programmes, are serving as automatic economic stabilizers, providing financial means to those who have lost their jobs or whose earnings have been reduced. They are also running large deficits that require increasing subsidies from state revenues, where debt is also mounting rapidly. In the low-income countries of South-Eastern Europe (SEE) and the CIS, unemployment benefits were cut significantly in the 1990s, both in terms of amounts paid and persons eligible. These gaps leave CIS and SEE workers without this critical first line of defence against economic hardship.

From this perspective, the duration of the global recession – and of its consequences, including the pace of job creation in the recovery – is of crucial importance. It will determine whether the current flow of unemployment benefits is sustainable, as well as how much the long-term deficits facing pension systems will be inflated by this economic downturn. Beyond the EU, an extended recession would have far worse consequences, posing threats of spiralling poverty, declining social cohesion and political instability.

The challenges for administrations

In the recent period, many countries have opened doors to the participation of private firms in the delivery of benefits, not least so for pensions and health care. In pensions this is being done through privately-managed individual savings accounts and in health care through private health insurance and medical treatment. Both types of reforms allow for multiple providers and, with regards to certain decisions, give beneficiaries a choice. Furthermore, some social health-protection schemes have organized market-like competition where public providers must compete for resources. In family benefits, governments are making payment rules more flexible for private childcare. A few are moving to substitute individual savings for social insurance-type family benefits, thus giving insured persons broader choice in how to use accrued savings i.e. for retraining, sabbaticals or childcare leave.

For insured persons, offering greater choice as regards benefits providers and individual benefits presents a requirement for the provision of better information. For social security policy-makers and administrators, reform approaches that permit multiple providers and accord greater choice in social security provision pose a set of difficult questions:

- How to provide individuals with meaningful and appropriately regulated choices while maintaining the requisite protection against the risks that social security systems are intended to address?
- How to preserve economies of scale inherent in a single unified national scheme?
- How to avoid an erosion of benefit adequacy as the result of higher administrative costs associated with moves towards more institutionally-fragmented social security provision?
- How to ensure that individuals have the skills and information necessary for making choices that result in enhanced welfare outcomes?

To a greater extent than before, “client-oriented” social security administrations are expected to provide improved public services and to coordinate their efforts with counterparts in other public agencies and with non-public delivery bodies. They must also inform policy-makers of any issues encountered in implementing reforms. Taken together, these elements make the task of social security administration more technically demanding.

Looking forward: Key policy messages

There is greater recognition that social security reforms in Europe must remain anchored in Europe’s social traditions while being better tailored to match evolving national environments. This outlook includes calling upon administrators’ experiences, perspectives and insights as inputs to policy deliberations. In turn, this gives administrators a responsibility not to wait to be asked, but to be proactive in sharing their views with policy-makers, especially as regards policy implementation – a stance that is fully consistent with the ISSA’s Dynamic Social Security framework and the emphasis placed on the need of social security administrations to be forward-looking.

Looking to the future, and taking into account the evolving roles and objectives of policy-makers and social security administrators in Europe, four key messages may be presented.

First, reform is increasingly complex and must be undertaken in a coordinated and tailor-made manner to pursue multiple goals (i.e. adequate coverage, quality of services, improved cost-effectiveness, pluralistic delivery mechanisms, appropriate regulation and governance, adjustment to demographic change) that are increasingly ambitious.

Second, movement towards evidenced-based policy-making requires systematic data collection and greater consideration must be given to the knowledge input to be offered by social security administrations. This requirement may differ according to the level of economic development of the country and the quality of its governance.

Third, to ensure the financial health of all programmes and the adequacy of benefits in a context of demographic ageing and shifting labour markets, and to improve service quality while offering the possibility of a greater degree of choice in benefits and services, all stakeholders have a responsibility to adapt their behaviour.

Fourth, the European “social model” has proven to be a robust and proactive instrument in meeting the challenges presented by the recent economic downturn. Its role in helping stimulate recovery across the region will be no less important. However, in a context of fiscal restraint, the longer-term financial challenge for social security programmes will be determined by the duration of the crisis and its lasting consequences, especially as regards the impact on employment levels and the pace of job creation. Nonetheless, the reaffirmed confidence about – and the growth in political support for – social security that has been witnessed gives cause for optimism.

To conclude, to make further progress towards what the ISSA calls Dynamic Social Security, well-informed policy choices and high-performing social security administrations are necessary but not sufficient elements. To reiterate, adaptation is also required in the behaviour of all stakeholders. To this end, social security administrations, the ISSA’s member organizations, are duty bound to lead by example.

Sources

- ¹ ISSA. 2010. *Dynamic Social Security for Europe: Choice and Responsibility* (Developments and Trends). Geneva, International Social Security Association.
- ² EC. 2009. *2009 ageing report: Economic and budgetary projections for the EU-27 Member States (2008-2060)*. Brussels, European Commission – Directorate General for Economic and Financial Affairs.
- ³ IMF. 2009. “Global economy contracts, with slow recovery next year”, in *IMF Survey Magazine*, 22 April. Available at <http://www.imf.org/external/pubs/ft/survey/so/2009/res042209a.htm> (accessed on 18.01.2010).

The **International Social Security Association (ISSA)** is the world’s leading international organization bringing together national social security administrations and agencies. The ISSA provides information, research, expert advice and platforms for members to build and promote dynamic social security systems and policy worldwide.

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