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SOCIAL SECURITY IN EUROPE: THE IMPACT OF AN AGING POPULATION

AN INFORMATION PAPER

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UNITED STATES SENATE

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PREFACE

Every student of social security knows that the population of the United States has been, on average, getting older and will age even more rapidly in the next century. These demographic forecasts have served to fuel the legitimate concern about the projected financial deficits of the social security program and its ability to meet future benefit commitments.

Yet, most Americans do not realize that Western European social security systems have already experienced the impact of an aging population for some time now. The Federal Republic of Germany, for example, currently has a ratio of social security contributors to beneficiaries of less than 2:1, which is the level not projected to be reached in the United States until the year 2030, when the postwar baby boom generation reaches old age.

Despite such demographic changes, the social security systems of Western European countries have not only survived, but they enjoy a level of public confidence among their citizens that probably exceeds the public confidence in the American system. This public confidence reflects the success with which these social security systems have been modified to meet the changing needs of the societies they serve.

This paper is a comparative study of the adaptation of the social security systems of the major industrialized countries of Western Europe to demographic changes that will also confront us. The author, Max Horlick, is a recognized expert who has spent his entire career studying international trends. This study is the latest of numerous books and articles he has written on international social security programs and pension plans.

In addition to the strictly demographic concerns, this study is also instructive because it illustrates the large extent to which social security around the world is a universal response to a common human need, namely, the need for economic security in the face of an uncertain economic world. In 1981, there were 139 countries with some form of social security, and 127 of these had some form of old-age, survivors, and disability program. Similarly, the historical expansion of social security in the United States and the improvements of benefit levels in the 1960's and 1970's were not unique to the United States. Indeed, as this study documents in abundant detail, all the major industrialized countries underwent a similar expansion of benefits and spending levels for social security.

By the same token, European countries are, like the United States, now experiencing both short-term and long-term financing problems. The short-term problems largely originated with the advent of recession and inflation after the oil crisis of 1973. The long-term problems relate to the aging of the population. Their response to both sets of problems is described in this study.

Unfortunately, the European experience, like almost everything else in the field of social security, does not lend itself to simple generalizations. Nor can we seriously expect that approaches taken by foreign countries would always be considered acceptable here in the United States.

Nevertheless, it is instructive for Members of Congress and the American public to consider the experience of other countries as we debate the future course for our own social security program.

Finally, we are struck, as probably every reader will be, with the durability of these social insurance programs. They have survived two world wars, ravaging inflation, and political and economic collapse. There is every reason to expect that the American social security system will display the same resilience, the same ability to guarantee economic security to all those who depend upon it, in both good times and bad times, if we commit ourselves to the goals it serves.

JOHN HEINZ,
Chairman.
LAWTON CHILES,
Ranking Minority Member.

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EXECUTIVE SUMMARY

The aging of the population, which is expected to cause financial problems for the U.S. social security system early in the next century, already exists in Europe today. Not only the unfavorable demographic situation, but also the prolonged recession, have put a strain on the social security systems of Europe, which may already be as severe as the financial strain predicted for the United States after the year 2015. Yet the social security systems have survived.

European countries generally foresaw the need to deal with a growing proportion of beneficiaries and a shrinking proportion of active workers to pay for the benefits. But their thinking did not anticipate two factors: the oil recession and continued social security program improvements. These factors, coupled with inflation, have led to an expansion of expenditures on income security programs to more than 25 percent of gross national product (GNP). Increased general revenue subsidies and higher payroll taxes have not been enough to overcome the social security deficits.

Beginning in 1976, the European countries facing the deficits began to take steps to bring in additional revenues, to slow the increase in expenditures, and to defer program improvements already decided upon. Cost containment measures included curbs on health insurance, modifications in the indexing of cash benefits and earnings histories, manipulation of reserve funds, some program cutbacks, and various technical changes to save money.

Steps taken to increase revenues included the removal of ceilings on payroll contributions, increasing the payroll tax rates for the self-employed, providing for contributions to social security by unemployment insurance funds in behalf of jobless workers, interfund transfers, special taxes (on alcoholic beverages, cigarettes, and automobile insurance premiums), and consideration of a tax on industries which are highly automated and use relatively few workers.

Despite the necessary steps to restore solvency to social security, there is also widespread agreement abroad that social security is a form of public expenditure that needs to be protected from wholesale cuts. Therefore, the tendency has been to make relatively minor changes and avoid any radical restructuring of the programs.

The financial outlook for these European social security systems is mixed. In the short term, the cost-containment and revenue generating measures have helped to alleviate the short-term deficits, and in some of the countries, the changes made were significant enough to restore the systems to financial surplus in the short term.

In other countries, however, the success has been less dramatic, and more work needs to be done, especially in the area of containing rising health care costs. The possibility of still another recession in the near term may compound the short-term financing difficulties of these countries.

Further ahead, the outlook will probably improve somewhat in the last two decades of this century during which the aging of the population will level off, temporarily. In the early decades of the 21st century, however, the European systems are expected to undergo another period of financial stress as the large, postwar generations attain retirement age. No concrete plans have yet been devised to deal with that second phase of aging. The European systems tend to do shorter range forecasts than in the United States (i.e., 15 to 20 year forecasts instead of 75 year forecasts), and they also attach far less significance to forecasts about the 21st century than do Americans.

Chapter 1

INTRODUCTION

After almost a century of sometimes intermittent development, European social security systems are encountering serious financial problems. These problems stem, in part, from an aging of the population, compounded by the continuing recession and inflation. European countries generally foresaw the need to deal with a growing proportion of beneficiaries and a shrinking proportion of active workers who pay for the benefits. Foreign planners could not, of course, foresee the oil-induced economic recession or predict that it would last as long as it has.

The very advanced stage of evolution of the European social security systems has resulted in high program costs. Revenues, however, have failed to keep pace. But, despite the dual challenge—an aging population and serious economic problems—the European systems have survived; and several of them recently succeeded in overcoming financial deficits. Although some countries have discussed the possibility of fundamental reorganizations, only minor adjustments have been introduced thus far.

The populations of most European countries have been aging since the post-World War II period. In 1950, the proportion of the population aged 65 and over in Europe was around 10 to 11 percent. By 1977, some countries had an elderly population of more than 15 percent. The primary impact on social security, of course, has been an increase in the dependency ratio, i.e., the proportion of beneficiaries to contributing workers grew.

While European countries had long been aware of the long-range demographic problem in financing social security, the inflation and recession of the 1970's caused short-range problems which had to be addressed immediately. The long-range and the short-range objectives sometimes conflicted with one another. For example, the increase in the elderly population suggested the long-term need to defer retirement to bring in more revenues for social security. On the other hand, high unemployment created the short-term need to encourage older workers to retire early. High employment occurred in countries which previously imported foreign workers to overcome labor shortages. For social security systems, unemployment meant lower revenues and higher outlays for the unemployed and their dependents.

Significantly, the recession of the mid-1970's followed a series of social security program improvements; programs had been expanding and improving since the post-World War II era. The oil crisis was preceded by an era of prosperity and economic optimism which led to further liberalizations, such as a lowering of the retirement age, the creation of flexible retirement, and so forth. The industrial countries experienced two decades of steeply rising social security expenditures.

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The volume of income transfers had risen as high as 30 percent of gross national product in some cases.

Rather suddenly, all of these forces converged, producing deficits for social security. The rising elderly population meant an increase in dependency on social security benefits and social services, paid for by a shrinking proportion of economically active workers. High levels of unemployment reduced revenues and further increased the demand for benefits and services. Inflation and the impact of the recent program improvements added to costs in a way that was not foreseen. To cope with deficits, the individual countries undertook a series of measures aimed at containing costs and restoring solvency.

This study focuses on eight European countries (Austria, Belgium, France, Federal Republic of Germany, the Netherlands, Sweden, Switzerland, and the United Kingdom), which have both the most developed social security systems and demographic problems. The experiences of other European countries are included where pertinent. Tables contain figures for the United States only for a point of reference. A period of 20 years is covered—1957–77. The timespan and the individual years for which statistics are available correspond to surveys made by the International Labor Office (ILO) in Geneva, Switzerland. This study sets out to accomplish four things: (1) To document patterns in the cost of social security for the years 1957–77; (2) to examine why these patterns emerged; (3) to learn what the countries have done about it; and (4) understand the implications of these patterns for those concerned with the long-term demographic problems.

This study is neither theoretical nor speculative. It deals with the past, rather than the future. The findings represent a summary of events and national debates and discussions, obtained from the literature of the individual countries and from meetings with individuals and groups there.

Chapter 2

THE RISING COST OF SOCIAL SECURITY

There has been a great deal of discussion in Europe about the rising cost of social security. National statistics show an ever rising level of income transfers and in-kind benefits, such as health care. The best way to measure these increases in an internationally comparable way is through the series of statistics issued by the International Labor Office (ILO) in Geneva, Switzerland. These statistics are published in the "Cost of Social Security," which is based on a questionnaire sent periodically to member countries since the 1940's. "Social security" in the international sense includes old-age, survivors, and disability programs, health insurance, worker's compensation, unemployment insurance, family allowances, public employee pension programs, and public assistance. To avoid confusion for American readers, the term "income security" will be used in reference to the broad, international definition of social security, and OASDI will be used to refer to the American usage of "social security," i.e., old-age, survivors, and disability insurance.

To show the trend over a 20-year period, published ILO figures for the survey years 1957, 1960, 1963, 1966, 1971, and 1974 were used. In addition, the social security department of the ILO kindly provided advance access to the most recent survey findings for the year 1977.

These statistics confirm a pattern which has been much discussed in Europe, that of a rather constant increase in expenditures for all of the programs, with, of course, a parallel need to increase revenues to finance them. Expenditures for social security cash benefits and other social programs have expanded considerably faster than the changes in consumer prices or in the gross national product (GNP).

TREND IN TOTAL EXPENDITURES

Table 1 and chart 1 show the trend in total expenditures for income security—or "social security" as broadly defined by the ILO—for eight European countries and the United States. The most striking points are: (1) The total expenditures of five of the eight European countries have risen to more than a quarter of GNP, varying from about 25 percent in Belgium to more than 30 percent in Sweden; (2) expenditures increased by 2 to 3 times since 1957, as a percentage of GNP; and (3) several countries, notably Switzerland, show a relatively lower level of expenditures, but all the countries spend more than the United States.

TABLE 1.—TOTAL EXPENDITURES FOR INCOME SECURITY PROGRAMS AS A PERCENTAGE OF GROSS NATIONAL PRODUCT, SELECTED COUNTRIES, 1957-77[1]

Country	1957	1960	1963	1966	1971	1974	1977
Austria	13.5	14.2	18.0	18.5	19.5	19.2	22.2
Belgium	13.1	15.1	15.2	16.4	18.4	20.7	25.4
France	14.3	13.7	15.4	16.6	(2)	22.4	26.5
Germany, Federal Republic of	16.6	16.2	16.9	18.4	18.8	22.5	26.5
Netherlands	10.4	11.1	14.4	16.9	21.5	24.7	28.4
Sweden	10.5	10.9	12.2	14.5	20.6	24.4	30.7
Switzerland	7.6	7.5	7.9	8.9	10.0	12.7	15.5
United Kingdom[3]	10.0	11.0	11.1	12.3	13.5	14.1	17.1
United States[3]	5.0	6.3	6.8	7.7	11.1	12.1	13.7

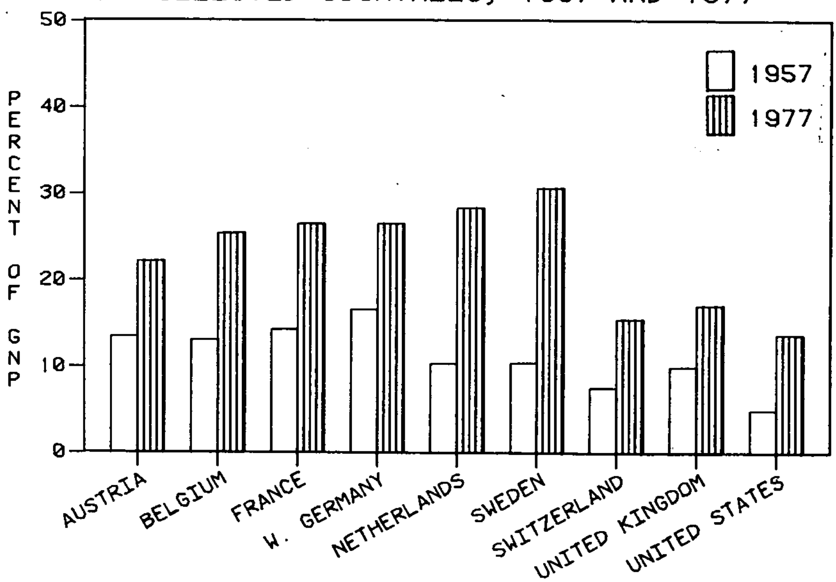
[1] These statistics are based on country data kindly provided by the International Labor Office and include old-age, survivors, and disability, public health insurance, worker's compensation, unemployment insurance, family allowances, public employee programs, and public assistance. Gross national product figures of the International Monetary Fund were used.

[2] Not available.

[3] Comparison adjusted to fiscal year.

CHART 1

TOTAL INCOME SECURITY EXPENDITURES AS A PERCENTAGE OF GNP SELECTED COUNTRIES, 1957 AND 1977



EXPENDITURES ON OASDI

Within the overall income security expenditures, the proportion devoted to old-age, survivors, and disability insurance (OASDI) is particularly pertinent to the American context. Table 2 and chart 2 show the percent of GNP devoted to expenditures on OASDI, using the U.S. definition. The figures cover national expenditures on cash benefits and exclude such items as supplemental security income, housing allowances, and other kinds of benefits included in European social security systems.

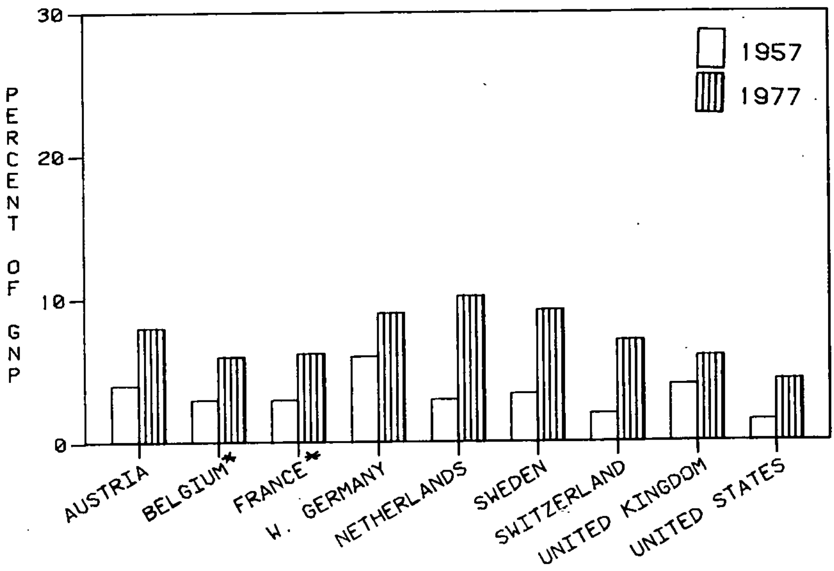
TABLE 2.—EXPENDITURES ON BENEFITS FOR OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE (U.S. DEFINITION) AS A PERCENTAGE OF GROSS NATIONAL PRODUCT, SELECTED COUNTRIES, 1957–77 [1]

Country	1957	1960	1963	1966	1971	1974	1977
Austria	4.0	5.0	5.3	6.0	7.0	7.0	8.0
Belgium [2]	3.0	3.1	4.0	4.0	4.2	5.1	6.0
France [2]	3.0	2.2	3.0	3.2	(3)	5.1	6.2
Germany, Federal Republic of	6.0	6.0	6.0	6.2	6.4	7.4	9.0
Netherlands	3.0	4.0	5.0	6.3	7.4	8.3	10.2
Sweden	3.4	3.3	4.0	5.0	6.0	7.1	9.2
Switzerland	2.0	2.2	2.3	3.0	4.0	5.3	7.1
United Kingdom [4]	4.0	3.2	4.0	4.0	4.0	5.0	6.0
United States [4]	1.5	2.2	2.6	3.4	3.4	4.0	4.3

[1] These statistics are based on data kindly provided by the International Labor Office, adjusted to include cash OASDI benefits. Gross national product figures of the International Monetary Fund were used.
[2] Disability insurance is administered together with sickness insurance and is not included.
[3] Not available.
[4] Adjusted to fiscal year.

CHART 2

EXPENDITURES ON BENEFITS FOR OASDI AS A PERCENTAGE OF GNP SELECTED COUNTRIES, 1957 AND 1977



* Disability Insurance not Included

The trend for OASDI expenditures is much the same as for the whole income security package. In 1957, six of the eight countries spent between 3 and 4 percent of GNP on OASDI programs. Switzerland was lowest with 2 percent and Germany highest, with 5.6 percent. All of the countries saw a continuing rise in OASDI outlays during the 20-year period. Costs tripled in three countries (Sweden, the Netherlands, and Switzerland), more than doubled in three others (Austria, Belgium, and France), and were 1½ times greater in Germany and the United Kingdom. In 1977, the portion of GNP devoted to OASDI cash benefits ranged from 7 percent in Switzerland to more than 10 percent in the Netherlands. The figures for Belgium and France are understated, since they do not reflect costs of the disability programs, which are administered together with sickness insurance.

Chapter 3

SOCIAL SECURITY REVENUES

The financing of European social security programs is carried out primarily through employer-employee contributions and general revenue subsidies. Other sources include earmarked taxes and yields from invested reserves.

PAYROLL CONTRIBUTIONS

Table 3 and chart 3 show total employer-employee contributions toward all income security programs as a percent of GNP. The different payroll tax levels do not, of course, take into account how much is provided from general revenue, a point discussed below. The differences between countries also reflect different philosophies and levels of benefits. It is not, however, these differences which are being emphasized here, but rather the similarity in trends.

TABLE 3.—TOTAL EMPLOYER-EMPLOYEE CONTRIBUTIONS TO ALL INCOME SECURITY PROGRAMS, AS A PERCENTAGE OF GROSS NATIONAL PRODUCT, SELECTED COUNTRIES, 1957–77

Country	1957	1960	1963	1966	1971	1974	1977
Austria	11.1	11.2	12.2	14.2	14.8	14.8	16.3
Belgium	8.9	9.2	10.1	11.6	12.9	13.9	15.2
France	10.8	10.6	12.0	12.5	(1)	16.5	19.4
Germany, Federal Republic of	11.2	11.0	11.8	11.8	13.1	15.0	16.2
Netherlands	10.1	10.3	12.8	16.6	20.2	22.9	23.3
Sweden	2.9	3.5	5.8	6.9	9.3	10.3	15.4
Switzerland	5.4	5.6	5.8	5.6	6.4	8.1	9.6
United Kingdom [2]	3.6	4.2	7.9	6.4	6.3	7.3	8.7
United States [2]	3.5	4.3	4.7	6.1	5.3	7.8	8.4

[1] Not available.
[2] Adjusted for the fiscal year.

There has been an overall increase in payroll taxes during the entire 20-year period, sometimes as a steady progression, sometimes in fits and starts, when a major change in a program or a new program was added. The payroll tax increases range from close to 50 percent (Austria and Germany) to 500 percent (Sweden). As of 1977, payroll contributions in six of the countries were more than 15 percent of GNP; Switzerland and the United Kingdom were in the 9 percent range.

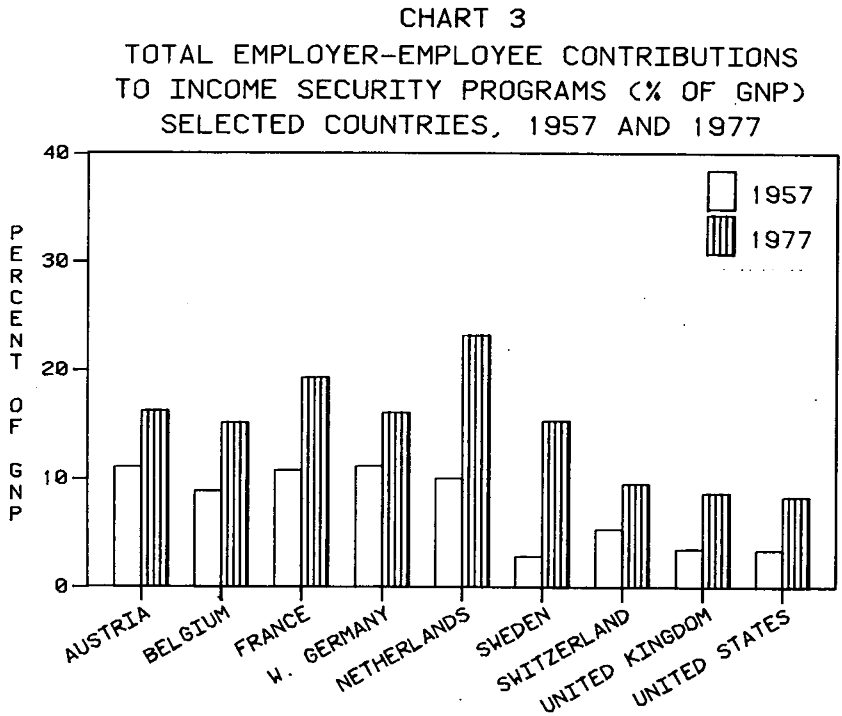


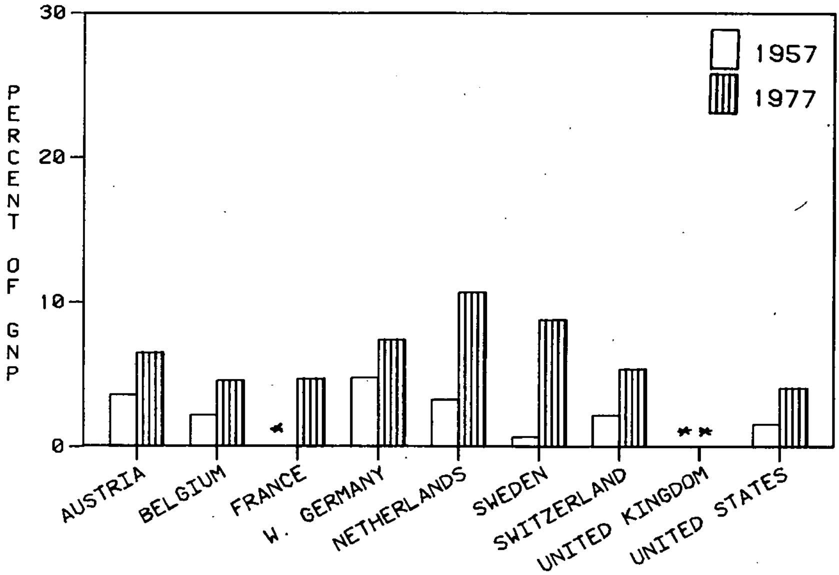
Table 4 and chart 4 separate out employee-employer contributions for cash benefits under old-age, survivors, and disability insurance (U.S. definition) as a percent of GNP. The pattern is the same as for the overall contribution rate. While the growth in payroll tax revenues in Austria and Germany is less than double, the increase in other countries was more than 200 percent and, in several cases, far more. While in 1957, the general range of payroll revenues was 2 to 4 percent of GNP, it had increased to around 5 to 10 percent by 1977.

TABLE 4.—TOTAL EMPLOYEE-EMPLOYER CONTRIBUTIONS TO OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE, AS A PERCENTAGE OF GROSS NATIONAL PRODUCT, SELECTED COUNTRIES, 1957-77

Country	1957	1960	1963	1966	1971	1974	1977
Austria	3.6	3.6	4.4	5.2	5.7	6.0	6.5
Belgium	2.2	2.1	2.5	3.0	3.7	4.3	4.6
France	(1)	2.3	2.5	3.0	(1)	4.1	4.7
Germany, Federal Republic of	4.8	4.8	5.1	5.2	6.6	7.5	7.4
Netherlands	3.3	3.4	4.6	5.8	7.4	8.7	10.7
Sweden	.7	1.4	3.4	4.0	5.4	5.4	8.8
Switzerland	2.2	2.4	2.5	2.5	3.1	4.7	5.4
United Kingdom [2]							
United States [3]	1.6	2.2	2.5	3.4	3.6	4.0	4.1

[1] Not available.
[2] Not separately available for OASDI.
[3] Adjusted to the fiscal year.

CHART 4
TOTAL EMPLOYER-EMPLOYEE CONTRIBUTIONS
TO OASDI (% OF GNP)
SELECTED COUNTRIES, 1957 AND 1977



* Data not available

The expanding costs of social security are directly reflected in the increases in payroll tax rates. As table 5 shows, for OASDI the payroll tax rates were relatively low in 1958, when the programs tended to be simpler and many programs were just evolving following the wartime period. Subsequently there were several major social security revisions, as well as continuous expansion of coverage and improvement of benefits. As a result of the benefit improvements, the aging of the population, and other factors, the payroll tax rates had by 1977 exceeded 20 percent in two instances. At the same time, the payroll tax for all income security programs was approaching as much as 50 percent of payroll.

Table 6 presents the 1981 payroll tax rates for all income security programs and for OASDI.

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TABLE 5.—OASDI CONTRIBUTION RATES, AS A PERCENT OF PAYROLL SELECTED COUNTRIES, 1957–77

Country	1958			1961			1967			1971			1975			1977		
	Employer	Employee	Total	Employer	Employee	Total	Employer	Employee	Total	Employer	Employee	Total	Employer	Employee	Total	Employer	Employee	Total
Austria[1]	6.0	6.0	12.0	7.0	7.0	14.0	8.25	8.25	16.5	8.75	8.75	17.5	8.75	8.75	17.5	8.75	8.75	17.5
	5.5	5.5	11.0	6.5	6.5	13.0	8.0	8.0	16.0	8.5	8.5	17.0	8.5	8.5	17.0			
Belgium[1]	4.25	4.25	8.5	4.5	4.5	9.0	7.0	5.5	12.5	8.0	6.0	14.0	8.0	6.0	14.0	8.0	6.0	14.0
	6.0	4.25	10.25	6.0	4.5	10.5	6.0	4.25	10.25	7.0	4.75	11.75	8.0	5.75	13.75			
France	10.0	6.0	16.0	13.5	6.0	19.5	15.0	6.0	[2] 21.0	5.75	3.0	8.75	7.25	3.0	10.25	7.7	3.45	[3] 11.15
Germany, Federal Republic of	7.0	7.0	14.0	7.0	7.0	14.0	7.0	7.0	14.0	8.5	8.5	9.0	9.0	9.0	18.0	9.0	9.0	18.0
Netherlands		6.75	6.75	(4)	6.75	6.75	(5)	(5)	(5)	4.0	12.7	16.7	6.15	14.95	21.1	8.65	15.55	[6] 24.20
Sweden		[7] 2.5	2.5	5.0	4.0	[8] 9.0	8.5	4.0	(9)	10.25	5.0	[10] 15.25	[11] 14.95		14.95	[12] 20.3		20.3
Switzerland	2.0	2.0	4.0	2.2	2.2	4.4	2.2	2.2	4.4	2.9	2.9	5.8	4.7	4.7	9.4	4.7	4.7	9.4
United Kingdom												(13)	8.5	5.5	14.0	8.75	7.75	[14] 16.5
United States	2.25	2.25	4.5	3.0	3.0	6.0	3.9	3.9	7.8	4.6	4.6	9.2	4.95	4.95	9.9	4.95	4.95	9.9

[1] Upper figure, tax rate for wage earners; lower figure, tax rate for salaried employees.
[2] Also finances sickness and maternity program; 1958, 1961, and 1967.
[3] Disability and survivor benefits financed under sickness and maternity program; 1971, 1975, and 1977.
[4] Employer pays monthly flat-rate contribution for disability; 1958 and 1961.
[5] Not available.
[6] Disability and survivor contributions also finance work-connected disability pensions; 1971, 1975, and 1977.
[7] Employee: 2 percent of assessable income for the universal pension.
[8] Employee: 4 percent of assessable income for the universal pension; employer: 5 percent of wages between the base amount and 7½ times the base amount for the supplemental pension (base amount January 1961, 4,000 SKr.).
[9] Employee: 4 percent of assessable income for the universal pension; employer: 8.5 percent of wages between the base amount and 7½ times the base amount for the supplemental pension (base amount January 1961, 5,600 SKr.).
[10] Employee: 5 percent of assessable income for the universal pension; employer: 10.25 percent of wages between the base amount and 7½ times the base amount for the supplemental pension (base amount January 1971, 6,400 SKr.).
[11] Universal pension: 4.2 percent of payroll; supplemental pension: 10.75 percent of wages between the base amount and 7½ times the base amount (base amount January 1975, 9,000 SKr.).
[12] Universal pension: 8.3 percent of payroll; partial pension: 0.25 percent of payroll; supplemental pension: 11.75 percent of wages between the base amount and 7½ times the base amount (base amount January 1977, 10,700 SKr.).
[13] For the years 1971 and before, contributions were based on flat rate amounts or a combination of flat rate amounts and a percentage of wages, and are therefore not comparable.
[14] Also finances medical services, cash sickness, maternity, work injury, and unemployment benefits.

Source: "Social Security Programs Throughout the World," 1958, 1961, 1967, 1971, 1975, and 1977 editions.

TABLE 6.—PAYROLL TAX RATES FOR SOCIAL SECURITY PROGRAMS (1981)

[As percent of payroll]

Country	All programs			OASDI		
	Employers	Employees	Total	Employers	Employees	Total
Austria	27.80	15.90	43.70	11.35	9.75	21.10
Belgium	27.77	10.10	37.87	8.86	6.25	[1] 15.11
Canada	[2] 4.49	3.95	8.44	1.80	1.8	3.60
France	37.41	10.14	47.55	8.20	4.8	[3] 13.00
Germany, Federal Republic of	17.95	16.45	34.40	9.25	9.25	18.50
Italy	47.57	7.45	55.02	17.31	7.15	24.46
Japan	12.22	9.85	22.07	5.30	5.30	10.60
Netherlands	29.575	28.075	57.65	12.90	22.0	[4] 34.90
Sweden	35.05	.15	35.20	21.15	----------	21.15
Switzerland	8.24	9.48	17.72	4.70	4.7	9.40
United Kingdom	13.70	7.75	21.45	(5)	(5)	(5)
United States	11.35	6.65	18.00	5.35	5.35	10.70

[1] Disability benefits financed through sickness insurance.
[2] Excludes work injury insurance.
[3] Disability and survivors benefits financed through sickness insurance.
[4] Disability insurance also includes worker's compensation.
[5] Not available.

Source: Comparative studies staff, Office of International Policy, Office of Policy, Social Security Administration.

GENERAL REVENUE

While the role of general revenue will be discussed in greater detail in chapter 5, table 7 shows that the percent of OASDI expenditures covered by general revenue fluctuated throughout the period, reflecting economic conditions and other influences on the social security funds. Some of the countries show a decreased proportion of general revenue over the years; some countries increased their use of general revenues; and some moved up and down. In 1977, general revenue covered less than 10 percent of costs in the Netherlands and France, less than 20 percent in Switzerland and Sweden, almost 25 percent of costs in Belgium and Germany, and 35 percent in Austria.

TABLE 7.—GENERAL REVENUE CONTRIBUTIONS TO OASDI AS A PERCENTAGE OF EXPENDITURES ON OASDI BENEFITS, SELECTED COUNTRIES, 1957–77

Country	1957	1960	1963	1966	1971	1974	1977
Austria [1]	15.9	20.3	28.3	32.0	29.4	30.0	34.8
Belgium	34.0	33.1	30.4	27.3	19.7	21.5	23.4
France	(2)	8.4	7.6	6.0	(2)	14.1	9.7
Germany, Federal Republic of	37.8	33.8	32.8	32.0	25.3	25.1	24.2
Netherlands	10.4	8.3	5.4	8.5	4.9	3.9	7.8
Sweden	62.3	43.9	53.1	61.1	50.6	49.4	18.82
Switzerland	17.3	14.0	14.7	19.4	20.2	18.8	14.76
United Kingdom [3]							
United States [4]	(5)	(5)	(5)	(5)	(5)	(5)	.8

[1] Cash benefits without housing and supplemental security income.
[2] Not available.
[3] Data not available.
[4] Adjusted for fiscal year.
[5] Negligible.

Table 8 shows that general revenue for all income security programs ranged from 20 to almost 50 percent of expenditures in 1977.

TABLE 8.—GENERAL REVENUE CONTRIBUTIONS FOR ALL INCOME SECURITY PROGRAMS AS A PERCENTAGE OF TOTAL EXPENDITURES, SELECTED COUNTRIES, 1957–77

Country	1957	1960	1963	1966	1971	1974	1977
Austria	17.4	21.2	20.3	21.6	21.3	20.5	21.9
Belgium	25.9	31.4	28.4	26.8	27.1	28.0	33.9
France	15.5	14.9	13.6	15.0	[1] 18.5	17.6	19.2
Germany, Federal Republic of	28.1	25.8	22.9	27.7	23.6	21.4	22.5
Netherlands	16.2	12.1	10.9	9.8	10.7	14.1	18.4
Sweden	46.1	40.5	41.6	43.2	35.4	37.5	22.9
Switzerland	9.5	9.7	8.8	13.8	14.6	15.7	12.4
United Kingdom [2]	54.5	53.6	43.2	43.8	47.3	45.2	47.0
United States [2]	25.8	21.7	26.0	27.2	28.8	28.1	28.4

[1] 1972.
[2] Adjusted for fiscal year.

Chapter 4

FORCES BEHIND EXPANDING COSTS AND FINANCIAL DEFICITS

AGING POPULATIONS

For many years, there was no particular concern about the expansion of expenditures for social programs. In fact, there were steady pressures for further improvements until deficits began to occur after the oil-induced recession beginning in 1973–74. Until then, there was little interest in analyzing why program costs were expanding to such a degree. Only in the health care field was there any serious thought of examining the causes of the rising costs.

As the recession persisted, however, and as some of the major systems struggled with increasing social security deficits, serious examinations were undertaken to determine what had been happening and what to do about it. A series of demographic, economic, and technical factors were blamed, including the aging of the population (although some of the discussants tended to minimize the current impact), longevity, early retirement, program improvements, indexing, the increased proportion of women in the labor force, and others. How these forces had operated in making expenditures rise faster than receipts was in many cases not altogether clear. In particular, the available statistical evidence regarding the impact of indexing, the increased proportion of women workers, earlier retirement age, and increased costs due to benefit improvements, left many questions unanswered.

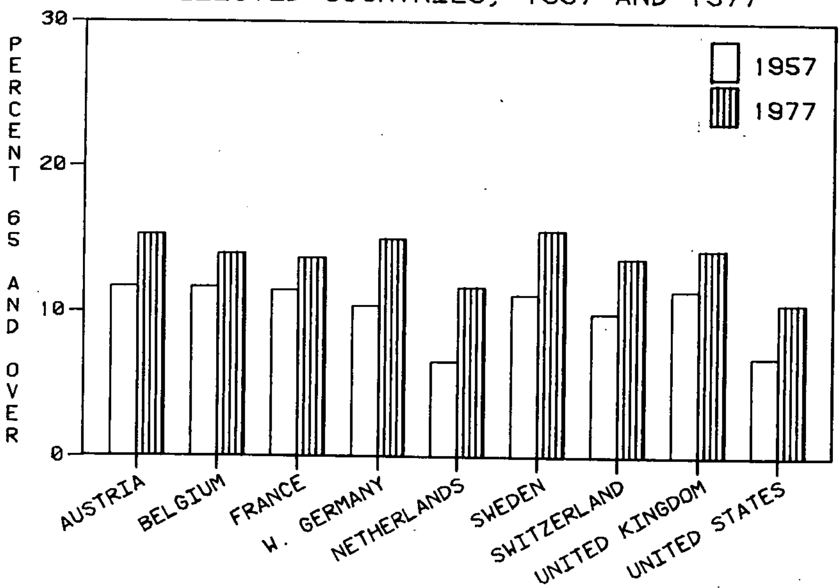
The aging of the population in the countries under study is shown in table 9 and chart 5, which show the population 65 and over as a percent of the total population. In 1957, about 10 to 11 percent of the population was age 65 and over. By 1977, the elderly had risen to about 14 to 15 percent of the population in most of the countries. It should be pointed out that these are internationally comparable figures and that the individual national estimates of the elderly population often tend to be higher. Nevertheless, the figures represent an increase in the potential number of beneficiaries of up to 40 percent. As actuaries point out, each additional percent increase in the dependency ratio roughly corresponds to an extra percent increase in expenditures. By this reasoning, the aging of the population has exerted a major influence in the pattern of OASDI expenditure increases shown in the preceding tables.

TABLE 9.—POPULATION AGE 65 AND OVER AS A PERCENTAGE OF TOTAL POPULATION, SELECTED COUNTRIES, 1957-77

Country	1957	1960	1963	1966	1971	1974	1977
Austria	11.7	12.2	12.8	13.4	14.3	14.8	15.3
Belgium	11.7	12.0	12.4	12.8	13.5	13.8	14.0
France	11.5	11.6	11.8	12.3	13.0	13.3	13.7
Germany, Federal Republic of	10.4	10.8	11.5	12.2	13.4	14.1	15.0
Netherlands	8.6	9.0	9.4	9.7	10.3	10.7	11.1
Sweden	11.2	11.8	12.3	12.9	13.9	14.8	15.6
Switzerland	9.9	10.3	10.3	10.7	11.5	12.2	13.7
United Kingdom	11.5	11.7	11.8	12.1	13.2	13.8	14.3
United States	8.9	9.2	9.4	9.5	9.9	10.3	10.8

Source: For 1971, 1974, and 1977 OECD, Labor Force Statistics 1967-78, Paris 1980. For 1963 and 1966 OECD, Labor Force Statistics 1963-74, Paris 1976. For 1957 and 1960 OECD, Labor Force Statistics 1957-68, Paris 1970.

CHART 5
POPULATION AGE 65 AND OVER
AS A PERCENTAGE OF TOTAL POPULATION
SELECTED COUNTRIES, 1957 AND 1977



SOURCE: ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT, LABOR FORCE STATISTICS, 1957-68, 1967-78 (PARIS)

The specific contribution of aging to the increases in expenditures for all social welfare programs is more difficult to calculate, but it involves higher health insurance costs, higher public assistance payments, and increases for other benefits and services. Increased longevity is also important, because benefits are being paid for ever longer periods of time. This general trend can be illustrated by figures and estimates available for France. In that country, there were reported to be 200,000 people age 85 and over in 1950. By 1975, this number had grown to 500,000. The figure for 1980 was estimated at

580,000 and, for the turn of the century, at 860,000. The total population is growing at only a small fraction of this rate.

Table 10 shows OASDI expenditures—in constant prices—per capita of population age 15 to 64, i.e., expenditures are related to the number of people of working age and the figures are adjusted for price changes. This table shows that even if prices had not changed since 1957, the cost of OASDI for each individual worker would have registered an increase of 400 to 600 percent in most of the countries. In Austria, for example, per capita expenditures were almost five times as high in 1977 as in 1957, in real terms. In Switzerland and the Netherlands, the increase was almost sevenfold.

TABLE 10.—EXPENDITURE ON OASDI PER CAPITA OF POPULATION AGE 15–64, IN CONSTANT 1957 PRICES, SELECTED COUNTRIES, 1957–77

[1957=100]

Country	1957	1960	1963	1966	1971	1974	1977
Austria	100	122.8	183.0	240.0	349.0	399.0	481.0
Belgium	100	115.9	149.4	180.0	275.3	375.1	439.0
France	100	85.9	131.0	155.4	(1)	337.8	439.3
Germany, Federal Republic of	100	133.5	150.9	190.8	256.7	320.9	397.6
Netherlands	100	135.0	185.0	289.5	429.4	514.9	676.5
Sweden	100	114.4	146.8	187.1	282.7	372.5	500.0
Switzerland	100	121.8	145.3	220.2	339.8	555.0	675.5
United Kingdom	100	97.0	121.0	142.1	150.0	183.7	222.6
United States	100	152.1	194.4	230.6	295.4	367.8	429.6

[1] Not available.

EARLY RETIREMENT

During the 20-year period under study, the retirement age was lowered in a number of the countries, at the same time that the population was aging and longevity growing. Apparently, foreign planners seriously underestimated the number of newly eligible persons who would opt for early retirement and the length of their time in beneficiary status.

The age of retirement has a dual impact on the financing of social security. The retirement age is not only the age when a worker begins to receive a pension but it is also usually the age when a worker stops contributing. Lowering the retirement age increases costs because the worker receives a pension over a longer period of time, and it decreases revenues by shortening the working career.

The European trend has been to lower the retirement age or make it more flexible. Sweden and Norway lowered their retirement ages to 65 and 67, respectively, during the 1970's. Early retirement options were made available in many countries for workers with long service or workers who performed "arduous" work. Flexible retirement was introduced in Germany and Sweden. Many workers, as a result of such provisions, are retiring as early as age 55. In Austria and Germany, the proportion of new benefits awarded to men before the "normal" retirement age increased from 5 to 6 percent in 1960 to more than 50 percent in 1976. In Sweden, early retirement claims rose from 9 percent of the total in 1967, to 21 percent in 1974. At the same time, fewer and fewer people work beyond retirement age. The labor force participation rates of the population 65 and over fell in Europe from 16 percent in 1955 to 8.5 percent in 1980.

The complex reasons for these trends are both social and economic. The standard of living rose constantly in postwar Europe, part of which was translated into increased leisure time for the worker by shortening the working career in favor of a longer period of retirement. Early retirement was also considered an appropriate compensation for workers, particularly blue-collar workers, who had contributed to social security for many years or who had performed difficult or even tedious work. Blue-collar workers tend to begin working earlier than the more-educated white-collar workers (age 18 rather than 23) and do work that is more physically demanding (mining, for example) or less interesting (assembly line work).

Another force behind early retirement and the low labor force participation rates of those 65 and over was the improvement in benefit levels. Workers could retire earlier and leave the labor force completely because benefits were more adequate to guarantee the worker and family a reasonable standard of living for the rest of his or her life. Complementary social services also improved during the postwar period.

The increasing unemployment of older workers between the ages of 55 and 65 also contributed toward the trend in earlier retirement. Many elderly unemployed workers took advantage of the new flexible retirement provisions in Germany and Sweden. From 1973 to 1980, the average retirement age declined by 2 years in Germany.

Finally, many countries extended unemployment benefits for the elderly worker until the worker would be eligible for a retirement pension. Voluntary early retirement was even encouraged in Belgium, for example, if a young worker was given the retiree's job.

By the mid-1970's, although pressures continued in some of the countries to lower the retirement age, the social security financing deficits precluded further action in this direction. Notably, Swiss voters in 1978 rejected a proposal to lower the retirement age for men from 65 to 60, and for women from 62 to 58.

PROGRAM IMPROVEMENTS

During the 20-year period, program improvements accounted for a large portion of the added expenditures. Economic growth was rather continuous, inflation was moderate, and, before the oil recession, the level of unemployment was almost insignificant. In fact, most of the countries under study had to import labor—the so-called "guest workers." While social security planners pointed out the growing impact of the aging population, policymakers were under no real pressure to worry about the expansion. In fact, improvement was the theme of the period, under the impetus of social and political movement toward the betterment of the health and welfare of the populations. There seemed to be no serious reason not to continue in this direction.

Program changes included major reorganizations, as well as continued evolution toward broader coverage, introduction of new features, and the raising of benefit levels.

Important new features were added by some of the countries during the 20-year period. This included the creation of an earnings-related social security benefit on top of the flat-rate benefit, in Sweden for example. Other countries added separate disability programs, as in Switzerland and the United Kingdom.

Cash benefits were greatly improved in many cases well beyond changes in the cost of living. One form of improvement was an alteration of the benefit formula itself. Thus, in France, the basic amount payable at the earliest retirement age (60) was increased from 20 to 25 percent of average earnings, and increments for each additional year worked were increased from 4 to 5 percent. Italy set a target of 80 percent of earnings for old-age and disability benefits. Minimum benefits were created or raised to relatively higher levels. Other countries also improved the disability benefit formula and added a constant attendance cash allowance for severely disabled people who needed an attendant. Partial disability benefits were also introduced.

Retirement and disability benefits were also raised in several instances by changing the period for which average earnings were calculated to bring the benefit levels closer to final pay.

What especially contributed to a long-range increase in the replacement rate was the method of revaluation of the worker's earnings record, which in some countries had the effect of raising all lifetime earnings to a level slightly above current earnings. Those countries which continued to require lifetime or at least long periods of coverage liberalized the granting of credits for periods when no contributions were made due to such factors as education, job training, unemployment, incapacity, fallout periods associated with the Nazi period and World War II, and other reasons.

Over the past several decades, significant program reforms in the disability area were implemented in a number of the countries, particularly Belgium, Finland, and the Netherlands. These legislative changes generally led to an increase in the insured population, a relaxation of eligibility requirements, a liberalization of disability definitions, and improvements in cash benefits. In view of the wide scope of the legislative changes, the disability programs in these countries had naturally been expected to experience some expansion. However, the marked extent to which the growth actually took place could not be attributed solely to the legislative revisions, but also to other tendencies, as well.

Increased demands placed upon workers by changing technology appear to have been translated into provisions for earlier retirement and into leading "technologically displaced" older workers into claiming a disability benefit. Periods of unemployment, and economic declines in individual industries, are also believed to encourage disability claims. Further, the aging of the population raised the likelihood of an increase in disability claims based on age-connected medical impairments.

Survivors benefits were also improved in most countries. Benefit levels were raised; the eligibility age for widows was lowered.

Significant improvements were also introduced in all the other income security programs: Means-tested programs, health insurance, unemployment, worker's compensation, and family allowances. This involved, for example, a longer duration of payments, shorter waiting periods, relaxed age requirements, and higher benefit levels.

EXTENSION OF COVERAGE

The European trend in social security has been to universalize coverage by bringing in previously uncovered groups and by merging separate funds into one principal program. Many groups were excluded when the original programs were developed because it was difficult to include them under the traditional financing agreement of employer-employee contributions, particularly the self-employed, apprentices, part-time workers, low earners, agricultural workers, students, and housewives. The rest of the insured have had to make up for the inadequate financial base of most of these groups.

Because apprentices, part-time workers, and other low earners have a limited capacity to contribute, all or part of their contribution is sometimes exempted, or they pay lower payroll rates. Through various means, particularly the minimum benefit, low earners often receive higher benefits than they would otherwise get. Nonearners, principally students and housewives, the latter traditionally only covered as dependents, have also been covered recently by way of free credits or voluntary contributions which are usually low. The reduced contribution capacity of low earners or nonearners is made up for by general revenues, special taxes, and additional contributions from the rest of the working population.

Perhaps the most significant extension of coverage occurred when a number of the countries set up "demogrant" programs covering all residents for a flat-rate OASDI benefit (Sweden, Norway, Finland, and other countries), as the lower layer of a two-tier system, the upper layer being an earnings-related benefit.

MATURING PROCESS

When new kinds of OASDI programs are established, a lengthy period of "maturing" may be required before full benefits are paid. A new system may pay full benefits after a period varying from 20 to 45 years. In the first year, the benefits may be one-twentieth, two-twentieths in the second year, until a full benefit is paid after 20 years. This means that expenditures will increase during the entire period and then, in principle, achieve relative stabilization. In Sweden, benefits for an average worker in manufacturing were about 30 percent of final pay in 1965. They rose to 59 percent in 1975, largely because of the maturing system.

Another aspect of maturing is that initially few workers will be eligible for a benefit or will be able to meet minimum requirements. As time goes on, however, more and more people become eligible for higher and higher benefits, until all potentially eligible workers are fully covered. The process is accompanied by a constant increase in total expenditures. Theoretically, the funding is fully planned in advance. That is, when the new kind of formula is established, the payroll tax is set at a predetermined rate which is intended to be sufficient for the entire period of maturity, provided the original assumptions hold true.

IMPACT OF INDEXING

In some European discussions, indexing has been cited as one of the reasons for the relative acceleration of expenditures for OASDI. However, the way in which indexing may have exerted such an influence is not always clearly explained. When automatic indexing is first introduced, there is, of course, an increase in expenditures as compared to before. However, these countries have had indexing for some time. Theoretically, there should be no net increase in costs from a longstanding adjustment process. In those pay-as-you-go systems which pay earnings-related benefits and which have tax bases adjusted according to wage trends, there should be a balance between increases in revenues and increases in benefit costs: As wages increase, more revenue accrues to the social security system and is applied to adjusted benefits. Where benefits are adjusted by price changes, particularly before the 1974 recession, benefits were supposed to go up by the Consumer Price Index, but receipts should have increased more with the faster rise in wages. In theory, that is.

Movements in pensions, earnings, and prices for selected countries for the period 1965–79, with 1965 as a base year of 100, are shown in table 11. In four countries which use wage indexing (Austria, France, Germany, and the Netherlands), benefits rose more slowly than wages in the period before the oil recession of 1974. This was an intended effect, brought about in part by a built-in lag in the adjustment process. After the beginning of the recession, however, benefits began to rise more rapidly than wages in three of the countries, which implied that expenditures grew faster than revenues based on the payroll tax.

TABLE 11.—MOVEMENT OF PENSIONS, AVERAGE WEEKLY EARNINGS, AND CONSUMER PRICES, SELECTED COUNTRIES, 1965–79

[1965=100]

Country and index	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978	1979
Austria:													
Pensions [1]	116	123	132	139	149	160	174	192	212	236	252	270	287
Wages [2]	120	128	138	149	169	189	213	246	279	305	330	249	369
Prices	106	109	113	117	123	131	140	155	167	179	189	196	203
France:													
Pensions [3]	112	121	140	154	171	190	206	234	277	325	378	420	460
Wages	112	126	140	153	169	187	224	264	299	338	380	426	478
Prices	105	110	117	124	130	138	148	169	189	207	226	247	273
Germany, Federal Republic of:													
Pensions [4]	117	126	134	142	151	165	184	205	227	252	278	278	291
Wages	107	113	127	144	158	170	189	205	216	237	256	269	285
Prices	105	106	108	112	118	124	132	141	150	157	162	166	173
Netherlands:													
Pensions [5]	120	124	141	148	171	193	225	251	293	339	367	399	420
Wages	116	126	139	155	176	202	230	265	298	324	355	374	396
Prices	109	113	122	127	137	148	160	175	193	210	224	233	243
Sweden:													
Pensions [6]	113	121	128	131	141	157	161	179	210	226	249	275	305
Wages	117	122	131	144	156	170	181	197	229	255	273	(7)	(7)
Prices	111	113	116	124	134	142	151	166	182	201	224	246	264
Switzerland:													
Pensions [8]	110	110	160	160	176	176	320	320	400	400	420	420	440
Wages	114	120	122	140	158	176	200	225	240	243	255	263	271
Prices	109	112	114	119	127	135	147	161	172	175	177	179	185
United Kingdom:													
Pensions [9]	100	101	101	125	125	150	169	194	250	333	383	438	488
Wages	109	117	127	144	156	180	206	244	297	337	365	421	488
Prices	106	112	118	125	137	147	160	186	231	269	312	338	383
United States:													
Pensions [10]	100	100	113	130	143	143	172	172	190	206	219	232	247
Wages	107	114	120	124	132	144	153	164	177	195	213	232	250
Prices	106	110	116	123	128	133	141	156	171	180	192	207	230

[1] Wage-related coefficient of indexing since 1966.
[2] Average monthly wage.
[3] Based on wage-related coefficient of indexing since 1965.
[4] General computation base through 1977. After 1978, benefit adjustment no longer reflects the increase in general computation base. For 1978, the benefit was not adjusted; for 1979, the adjustment was limited to a 4.5-percent increase.
[5] Increase in flat-rate benefit amount for single pensioners.
[6] Increases in universal pension only; excludes earnings-related pension.
[7] Data not available.
[8] Based on increases in the minimum benefit amounts; indexing instituted in 1969.
[9] Increases in flat-rate benefit amount for single pensioner; based on ad hoc adjustments until 1971.
[10] Based on percentage increases in benefit. Indexing based on price, implemented in June 1975.

The pattern that emerged in four of the countries was a faster increase in benefits than in the indexes on which they were based, throughout the entire period. This was the case with a country using a price index (Sweden), a country using a price index and then switching to a combination of wages and prices (Belgium), a wage index (the Netherlands), and ad hoc adjustments (Switzerland). In these four countries, ad hoc adjustments played a significant role. That is, the indexing was not automatically made according to the amount of change in prices or wages, but was revised upward in addition for various policy reasons. Primarily, there was a desire to push up benefits, particularly the lower range of benefits, in order to achieve greater "adequacy." The increase in the minimum benefit was counted upon to decrease the role of supplemental security income-type payments and other means-tested benefits.

Another factor which had a negative impact on the balance between receipts and expenditures was the timing of the indexing process in some of the countries. That is, benefits were adjusted more frequently than the payroll tax. In Belgium, for example, there have been as many as five benefit adjustments in a year, while the contribution rates and ceilings were not raised as rapidly.

Chapter 5

MEASURES TO RESTORE FINANCIAL EQUILIBRIUM

By the mid-1970's, a number of the industrial countries began to face social security deficits for the first time in the postwar period. The more rapid increase in expenditures than of income became a cause for concern, as did the adverse effect of the rising cost of social programs, like social security, on the competitive position of their products and services on the world market. The recession greatly increased unemployment in countries which, in past years, had experienced labor shortages. To the social security systems, unemployment meant both lower revenues coming into the system and higher outlays from the system for the unemployed and for their dependents. As pointed out in chapter 4, the indexing of wage records plus numerous ad hoc adjustments were responsible for accelerating outlays. Even where there had been long-range planning, the cumulative effects of benefit improvements and the severity of a recession had not been foreseen.

Beginning in 1976, the countries facing the deficits began to take steps to bring in additional revenues, to slow the increase in expenditures, and to defer program improvements already decided upon. Notably, no radical changes were made and the feeling everywhere was that social security should be protected. A rather long list of measures included an increase in contributions and in general revenue subsidies, and various technical modifications. Primarily, the benefit containment was in health insurance. In OASDI, probably the most significant steps involved changes in indexing.

PAYROLL TAXES

All of the countries raised contribution rates. Three of them (France, Germany, and Switzerland) removed all or part of the payroll tax exemptions (primarily for health insurance) previously enjoyed by certain workers or pensioners over 65. Germany not only scheduled payroll tax increases for the future, but decided that if average earnings fall below long-range estimates, then additional increases in contribution rates or limitations on benefit expenditures would be required. France proposed increases in special taxes (on automobile insurance, tobacco, and alcohol) which help finance health insurance. Belgium introduced a tax on automobile insurance premiums and also increased the tobacco tax to help alleviate revenue shortfalls in the health and disability programs.

Over the years, as shown in table 7, the payroll tax was increased as programs were expanded or new programs were introduced. In retrospect, critics subsequently said, however, that many of the improvements had not been accompanied by commensurate increases in revenues to pay for them. Nonetheless, as long as the economies continued to grow at a high rate and real incomes improved, there was no particular public concern with the size of the payroll tax. After 1974, when economic growth slowed and real incomes grew more slowly or even declined in some years, the payroll tax continued to be increased for OASDI as part of the effort to solve its financial problems. By 1979, the combined employer-employee contribution was at or near the 20-percent level in most of the countries.

Between 1971 and 1979, the United Kingdom and Sweden doubled the payroll tax. It went up 47 percent in France, and 68 percent in the Netherlands.

In most European countries in this study, the employer pays a larger share of the payroll tax than the employee. Payroll tax increases have also generally been higher for the employer. Some have argued that this trend has increased the cost of labor and discouraged employment. The payroll tax increases particularly affect labor-intensive industries more than capital-intensive ones, encouraging a switch from labor to capital. Awareness of this situation influenced several of the countries to increase the employee contribution rate proportionately more than for the employer's and to offer payroll tax exemptions for employers to encourage employment. Because of the need to raise more revenue without discouraging employment, a number of countries discussed the possibility of introducing a tax on capital intensive industries, a procedure already adopted in Finland. There, capital intensive employers are taxed at a higher rate than labor-intensive companies.

Some of the countries raised the OASDI contribution rate for special groups, including the self-employed. Coverage of part-time workers was extended in Germany by lowering the minimum contribution requirement from 3 to 2 months and lowering minimum taxable earnings. One of the countries which did not previously require old-age beneficiaries to pay a payroll tax while working has removed the tax exemption on earnings above a certain amount. In Germany, with the beginning of the recession, the unemployment insurance funds were required to make contributions to OASDI on behalf of unemployed workers.

In addition, some countries which did not require pensioners to contribute for health insurance now require them to do so. In France, for example, as of 1981, pensioners contribute 1 percent of social security benefits and 2 percent of private pensions for health insurance. Pensioners with low incomes, however, are exempted.

In 1980, Belgium also added a health insurance contribution from pensioners—1 percent of their pension—unless their income is below a specified level.

PAYROLL CEILING

The ceiling (maximum earnings on which contributions, benefits, or both are paid) was manipulated in various ways with the aim of increasing revenues to the systems. The maximum amounts are normally indexed for wage or price changes. While the timing of the adjustments is set by law, the amount of the increase can be influenced by a consultative body in most of the countries, or there can be special legislation to modify the procedures. The consultative body can slow the growth by spreading sudden jumps over a number of years, or can take measures to accelerate the growth of the ceiling to bring additional earnings within the taxable limit. Before the 1974 recession, payroll tax ceilings were generally rising less rapidly than earnings, but this has since been reversed in some of the countries. In Austria, for example, the ceiling on earnings subject to payroll tax rose about 50 percent more rapidly than average covered earnings in 1975–79. An ad hoc increase in the ceiling was added to the automatic indexing.

Another kind of manipulation occurred in Germany. In most countries, the same ceiling on earnings applies to payroll taxes and to benefit computations. Proportionate increases in wages, in benefits, and in the ceiling were intended to keep income and expenditures in balance. Germany, however, took steps to disconnect the two functions. It put a cap on the adjustment of earnings levels for benefit computation purposes, but allowed the ceiling to increase automatically for contribution purposes.

The payroll tax ceiling was abolished for certain programs in Belgium, particularly for family allowances and for health insurance.

Table 12 and chart 6 show the impact of recent policies raising the contribution ceiling rapidly to increase taxable wages and produce more income for the system. In the period 1974–79, the ceiling was pushed up more rapidly than either wages or prices in almost all of the countries.

TABLE 12.—PERCENTAGE INCREASES IN OASDI CONTRIBUTION CEILINGS, WAGE LEVELS, AND CONSUMER PRICE LEVELS, 1971–74, AND 1974–79, SELECTED COUNTRIES

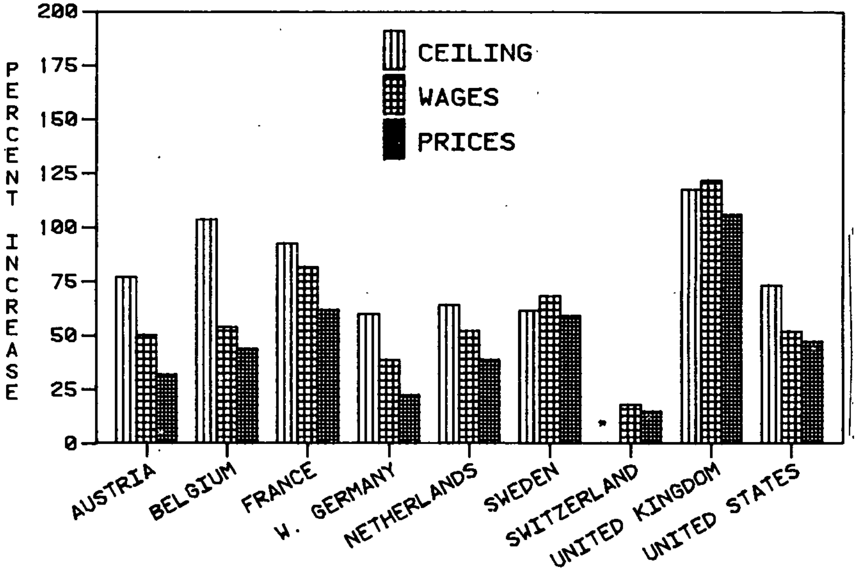
Country	1971–74			1974–79		
	Ceiling	Wages [1]	Consumer prices	Ceiling	Wages [1]	Consumer prices
Austria	29.6	45.6	25.2	77.1	50.3	31.9
Belgium	56.8	53.7	27.1	103.8	54.1	43.9
France	40.6	50.5	29.6	92.7	81.8	61.9
Germany, Federal Republic of	31.6	30.0	20.7	60.0	38.9	22.6
Netherlands	42.3	71.1	27.6	64.3	52.2	38.8
Sweden	17.4	27.0	24.3	61.7	68.4	59.1
Switzerland [2]		57.0	35.7		18.2	15.1
United Kingdom	47.6	61.6	35.6	117.7	122.0	106.1
United States	69.2	23.8	21.8	73.5	52.1	47.4

[1] Average wages in manufacturing.
[2] There is no earnings ceiling for contribution purposes in Switzerland.

Source: Country sources for the ceiling levels; ILO Yearbook of Labor Statistics, 1980, for wage and price changes.

CHART 6

PERCENT INCREASE IN OASDI CONTRIBUTION CEILINGS,
WAGE LEVELS, AND CONSUMER PRICE LEVELS
SELECTED COUNTRIES, 1974-1979



* Switzerland has no earnings ceiling for contribution purposes
SOURCE: ILO YEARBOOK OF LABOUR STATISTICS, 1980 AND COUNTRY SOURCES

GENERAL REVENUE

Of the eight European countries under study, six make substantial general revenue subsidies to OASDI, as shown in table 7. Two of the countries (France and the Netherlands) make relatively small contributions, and then only to special programs. As the countries experienced deficits and/or a decline in the growth of revenues, the tendency was to increase the general revenue subsidy. However, although the subsidy was considerably increased in cash terms, expenditures on OASDI also rose very rapidly.

There are some variations in the long-range patterns and these are due in part to the way the countries view general revenue subsidies. Generally, there are four major approaches: An annual subsidy which is fixed by percentage or amount; the provision of a sufficient amount to make up for deficits; the determination of a percentage each year; and general revenue support only for special funds or purposes.

The fixed amount or percentage approach is illustrated by Belgium and Germany. In the former, the Government's contribution to OASDI was set at a specific cash sum, which was to be inflation-adjusted and, in addition, to increase by 6 percent a year, beginning in 1970. As tables 7 and 8 show, the level of general revenue subsidies rose to over 23 percent for OASDI and to nearly 34 percent of expenditures for all programs by 1977. In recent years, the Government's general revenue contribution fell well below the amount required by the formula and well below the Government's commitment to make good the shortfalls of contributions for the last 4 to 5 years. There was a feeling among various segments of the society that the limits of the general revenue subsidy might have been reached and even exceeded, and that the competing needs of other programs could prevent the Government from maintaining its general revenue subsidy in the future. In October 1980, a broad-based political coalition came about because the Conservative Party refused to accept a larger general revenue subsidy.

Germany's general revenue subsidy was established in 1957, and was supposed to be based on a rigid formula. In practice, the subsidy policy has been flexible. During recessions, if the Federal budget is especially in need of revenue and the pension funds are solvent, the Government may reduce the amount or defer payment. The German figures in tables 7 and 8 show that the portion of OASDI costs covered by general revenue has been declining. The general revenue contribution for all of the income security programs, however, moves up and down in response to the economy. For example, the figures show increases during recessions in 1966 and 1977.

Austria and the Netherlands provide examples of how program structure and philosophy influence the amount of the general revenue subsidy. The principal purpose of general revenue subsidies in both countries is to make up any operating deficits. In Austria, it is considered that the general revenue contribution expresses social solidarity and consequently the subsidy has approached a third of costs. As can be seen from table 7, the Austrian Government's contribution to OASDI was more than 29 percent of total expenditures in 1971, before the recession, and has since risen to about 35 percent of a considerably expanded total cost.

The Swedish Government contributes only to the universal first layer of its two-tier social security program, making up for expenses not covered by employer payroll contributions. As table 7 shows, the Government's general revenue share has been declining for over a decade. This is because the financing has been shifted to employers. In 1971, general revenue covered 70 percent of the cost of the universal benefit, the rest being covered from a tax on the worker's "assessable" earnings. Subsequently, this tax was abolished and a payroll contribution was assessed on the employer alone. As this employer contribution has been increased. the general revenue share fell to 43 percent of the cost of the universal benefit in 1979.

Instead of having a predetermined amount or formula, Switzerland fixes the amount of general revenue subsidy by annual legislative changes. As table 7 shows, the subsidy had reached more than 20 percent of OASDI expenditures by 1971. An actual increase to 25 percent of annual expenditures had been planned as of 1978. Instead, due to the adverse effects of recession and inflation, temporary "emergency" measures in 1975 lowered the general revenue subsidy for the next few years and raised payroll taxes. The 20-percent general revenue subsidy is scheduled to be restored in 1982.

INTERFUND TRANSFERS

Many of the European countries have separate funds serving different occupational groups for OASDI, such as funds for blue-collar and white-collar workers. In the highly industrialized countries, the number of blue-collar workers has been declining as a result of economic and technological changes and because many jobs have been reclassified from blue-collar to white-collar status. Consequently, the white-collar component of the social security program has gained additional contributors while the number of workers supporting the blue-collar component has declined. This trend has been aggravated by the recession and by the growth of the aged population. White-collar social security funds have tended to be better off and to be operating at a surplus; the blue-collar funds have tended to operate at a deficit. Contributions can no longer pay for benefits within the declining sectors. To make up the shortages, white-collar funds have been required to make transfers to the blue-collar funds. In France, also, the general social security system had to transfer sizable funds to special occupational systems which were operating at a deficit, such as the agricultural fund.

In addition, the Belgian and French family allowance programs, which habitually enjoy a surplus, have been required to help the old-age pension funds and also health insurance. In France, each of the main components of the general social security system independently prepares annual estimates of its income and expenditure. It has been the custom, when one fund's expenditures exceed its income, for that fund to receive a transfer or subsidy from another component with a surplus. This transfer usually went from the family allowance fund to the health insurance fund and occasionally to the old-age pension fund. This type of transfer is not always direct. For example, in January 1974, the family allowance contribution rate was lowered by 1.5 percentage points and that part of the contribution applied instead to the old-age insurance fund. Legislative action is required in order to transfer contributions from one component to another within the general system.

In Germany, the unemployment funds now must contribute to the pension funds on behalf of the unemployed. Requiring pensioners to make contributions for sickness insurance, as they now do in France, Belgium, and, in the future, in Germany, is indirectly a transfer from pension funds to sickness insurance funds. The direct subsidy from the pension insurance funds to the sickness insurance funds has also been reduced in Germany.

USE OF RESERVE FUNDS

Most European countries finance social security using the pay-as-you-go system that requires only a small contingency reserve fund. The contingency reserves in European countries have varied from a high of 4½ years of current expenditures in Switzerland in 1966, to a low of 1.5 percent of annual expenditures in Austria before 1977. Austria increased the reserve requirement after 1977 to a little less than 1 month's expenditures. Such a small fund is possible if general revenues are available to make up any deficit, as they are in Austria.

In most of the pay-as-you-go systems, modest contingency reserve funds were planned. Contribution rates were initially set higher than needed, or a long maturing period was planned before full benefits were paid. As a result, reserve funds were built up in the early stages of the program, while pensioners were few and benefits low, with a subsequent decline as expenditures overtook contributions. The reserve funds were also considered as buffers against short-run economic fluctuations and the aging population.

The post-1974 economic slowdown coincided with a peaking of the aging process and the maturing of the social security systems. The contingency reserve funds in most countries, consequently, have declined. In Germany, the reserve fund has dropped from the equivalent of 9 months of payments in 1974 to about 1.5 months of payments in 1980. In Switzerland, in the 10-year period 1966–75, the size of the reserve fund in terms of current expenditures declined from 4 years and 5 months to 1 year and 2 months, and it continued to deteriorate in 1980. Between 1975 and 1980, the reserves in Belgium's national employees pension fund have declined from 5.5 months of expenditures to 1.7 months.

In the United Kingdom, the reserve fund remained relatively stable, averaging 4.4 months of expenditures between 1971–77. This stability reflects, in part, that all social security programs are lumped together and deficits and surpluses in different programs balance each other out.

Only Sweden planned to have a large reserve fund when it instituted the earnings-related pension in 1960. The reserve fund was considered necessary to avoid large increases in contributions when the program became fully mature in 1990, and also to smooth out the effects of the aging population. The rapid rate of inflation in the post-1974 period has been eating away at the projected value of the income from assets faster than expected. However, the size of the fund is no longer determined by the needs of the pension system. Since the fund is now the chief source of investment capital in Sweden, its eventual liquidation is unlikely. The pension system may not be fully funded in an actuarial sense, but it will have a permanently large reserve.

INDEXING

As mentioned earlier, all of the countries had some form of automatic adjustment of benefits before the 1974 recession. Wage indexation was regarded as better than price indexation because it included productivity improvements. As prices began to outstrip wage increases in the mid-1970's, however, there were pressures to switch from wage to price indexation, and a number of countries began to base their adjustments on some combination of both wages and prices. As the main systems went into deficit, there were debates about reversing this trend for improvement and limiting the impact of indexing, if only temporarily. In fact, indexing came to be viewed as a political, not an actuarial, process. Rather than modifying the benefit directly by changing the benefit formula, the countries made indirect reductions in benefits through changes in indexing. This was done by placing a temporary cap on adjustments (Germany and Italy), by splitting the cost-of-living adjustment into two parts—a portion indexed and a portion flat rate (Belgium)—and simply making an adjustment which is less than the one called for by the indexing formula (the Netherlands).

The strongest measure was Germany's capping of the annual benefit adjustment for 1978–81, and its permanent shift in the benefit adjustment payment date from July to January. In 1980, Germany achieved a small surplus in its social security funds for the first time since the 1974 oil recession, and "consolidation measures" such as the indexing cap were credited with bringing this about. Italy also used a kind of capping. There, all beneficiaries are given a flat-rate adjustment reflecting price increases. In addition, a percentage increase is given that reflects an average of wage and price rises. In 1979, Italy limited the second step in the adjustment to an increase of 2.9 percent, instead of 5.9 percent.

Since 1976, the cost-of-living adjustment in Belgium has been at a flat rate. This means a high percentage benefit increase for those receiving small pensions and a lower percentage increase for those receiving higher ones. The measure was seen as protecting the adequacy of retirement benefits for the most needy while producing an overall savings for the social security system. The new procedure is considered temporary and its continuation is decided on an annual basis. Also, a draft bill would put a temporary halt to the indexing of the highest social security benefits.

Cutting down on the amount of indexing is also illustrated by several other countries. In the Netherlands, the Government may make smaller increases than called for by the wage pattern or it may delay the full implementation of the increase.

In the United Kingdom, since May 1980, social security benefits are no longer linked to the higher of the increases in wages or prices (1975 law), but rather only to prices. It has also been proposed to limit indexation to the lower of wages or prices. Also, disability, unemployment, work injury, and maternity benefits are adjusted 5 percentage points less than price rises since November 1980, and social security benefits in 1981 are being adjusted by 1 percentage point less than the automatic adjustment provision.

Since 1978, Germany and Switzerland have also modified the revaluation of earnings histories for benefit computation purposes to bring about relatively lower benefit levels. In Germany, the computation of a benefit is based on a uniform national average wage figure. This figure, in turn, moves upward annually according to increases in average covered earnings. In July 1978, however, the national average wage figure was increased only 4.5 percent instead of the full amount of the wage increase (8.5 percent). The next increase at the beginning of 1980 was held at 4 percent instead of 7 percent, and the 1981 increase was limited to 4 percent instead of 7.4 percent.

In Switzerland, the earnings records of all beneficiaries had been revalued at one uniform rate. Beginning in 1979, however, this was changed so that the longer the period of covered service, the higher the amount of revaluation. For example, people working since the beginning of the system in 1948 would have their earnings doubled (multiplied by 2.1) and there would be a descending scale down to zero revaluation for those covered only in 1972 and subsequent years. The rationale for such a change was that a single indexing rate for all workers assumed a complete history of contributions. This tended to favor those who contributed only a short time before retiring because the average annual earnings of an individual with a short contribution history would be relatively greater than that of a worker contributing for many years, since the latter would have had to average in the lower wages of the late 1940's and early 1950's.

While some countries switched from a wage to a price index, or combined the two, only one—Sweden—changed the nature of the index it was using. There, the price index was modified in 1981 by dropping from the index both indirect taxes and changes in the price of energy.

DEPENDENTS

Cost-containment measures were also applied to dependents benefits, particularly through more stringent entitlement requirements and/or direct or indirect reductions in benefits. One form of stricter entitlement was the tightening of the definition of a dependent child. Revised regulations were issued in Germany regarding the classification of foster children and dependent nieces, nephews, and younger brothers and sisters. Benefit eligibility for older children was tightened by establishing an income test for orphans (in Austria), and for all dependent children above age 17 (in Germany). Formerly, the families of students and trainees over 18 in Germany received cash monthly allowances no matter what their income was.

The automatic adjustment of family allowances was also stopped in Germany. It was halted for the first child in the Netherlands and for supplements for dependent children of beneficiaries in Austria. In Denmark, family allowances were reduced for children under 16 and eliminated for children between 16 and 18 if their families are in a high income group. Supplements for dependent children were reduced in the United Kingdom and the maximum amount of the child's supplement for pensioners was lowered in Austria.

Another approach was that of the Netherlands, where the family allowance program was restructured by increasing the payments for the first three children in exchange for the elimination of tax exemptions on the income from family allowances. A savings in expenditures was anticipated.

There was also a tightening of the age of eligibility for a dependent wife's supplement to an old-age benefit. In Switzerland, the age of eligibility is being gradually raised in 1 year steps from age 45 to 55, and the amount of payment reduced. Previously, a supplement of 35 percent was paid for wives age 45 to 60. Now, only 30 percent is being paid. The supplement previously went up to 50 percent at age 60; now the increase occurs at age 62.

Another measure affecting dependents was the elimination of multiple benefits under different programs in Austria and Switzerland. Also, Belgium and Germany eliminated the possibility of receiving both an orphan's benefit and a dependent child's supplement to an OASDI or work injury pension.

DISABILITY

There were only a limited number of changes in the disability insurance area, with only one reform of major significance proposed—in Italy.

That country proposed to reduce the growth in the number of permanent disability pensioners by subdividing the existing program into temporary partial disability and permanent total disability. The definition for permanent total disability would be more stringent than the existing one (100-percent disability in contrast to the present 66⅔ percent requirement). This change would be intended to discourage people who are not totally disabled from coming on the rolls permanently. Belgium has given thought to introducing partial disability for the same reason.

Dual entitlement to disability and unemployment benefits has been restricted in Germany and in the United Kingdom and similar restrictions were proposed in Belgium. In Germany, the work injury pension was cut if unemployment benefits were being received simultaneously and unemployment benefits were cut if a general disability pension was being received. Unemployment benefits for those retired on substantial occupational benefits will also be reduced in the United Kingdom. The Netherlands has delayed extension of a new basic disability benefit to women receiving a survivor's benefit, and the United Kingdom has indefinitely postponed the introduction of a noncontributory disability pension for housewives.

OTHER COST-CONTAINMENT MEASURES

The French Government now requires companies with at least 400 workers to deposit contributions within 5 days following the month for which they are owed—instead of 15 days. The Swiss recently began to charge interest on delayed payment of contributions.

Under programs receiving general revenue support, several countries made benefits subject to income tax (Belgium: disability and unemployment benefits; France: cash sickness benefits; Australia: widow's sickness benefits and unemployment benefits).

MANDATING PRIVATE PENSIONS

While social pressures for higher benefits continued in all of the countries, the role of the private sector in meeting such pressures began to be explored in Switzerland and the Netherlands, particularly. There, it was felt that increases in the payroll tax, the ceiling on earnings subject to social security tax, and general revenue subsidies could not be sufficient to finance the desired replacement rate. In these two countries, the need for private supplements to social security was tentatively decided upon. It was expected that a combined social security/private pension benefit would be high enough to attain the long-promised objective of enabling retired workers to maintain the standard of living that they had when they were active. An additional advantage seen by the proponents of mandating private pensions was that funds channeled through the private sector would contribute directly to savings and investment, while an additional layer of social security would not. The implementation of mandatory private pensions was, however, deferred in both countries because of the economic problems following the recession.

It should be pointed out that France and Sweden, among others, already have very broad private pension coverage which is almost tantamount to mandating. This was achieved, however, through labor/management negotiations within the historical contexts of those countries and with very little—if any—Government role.

Chapter 6

IMPLICATIONS FROM THE EUROPEAN EXPERIENCE

Significant implications for the future can be drawn from these patterns of the past. The chronological progression of developments may be viewed as follows: The major systems were revised after World War II. The revisions involved planning ahead, the number of years of advance planning varying with the country and type of system. Only a few countries took a very long-range look ahead, and that was primarily aimed at the "maturing" process of 40 to 45 years. Two of the countries, Sweden and Switzerland, provided for the building up of a sizable reserve fund to compensate for a maturing social security system and for an aging of the population. Early in the postwar period, it was Germany which was most concerned with the aging process and it is, symbolically, the only country which has a word for it: the *Rentenberg*. Other countries did not tend to take a long-range view, and there was nothing like the 75-year projections in the United States.

The second period of development involved the expansion of the programs and the improvement of benefits. This continued up to 1974 and sustained the pattern of advancing social programs which had begun with the Bismarck era. Decisions were made and legislation promulgated in an atmosphere of optimism and of favorable forecasts regarding inflation, economic growth, employment, and the financing prospects for social security. These proved to be well founded in the short run and the expansions were accompanied by constant surpluses.

The third period, starting in 1974, saw recession, inflation, and, for the first time since World War II, social security deficits. The countries faced not only a very significant deterioration in the ratio of beneficiaries to active workers, but general economic problems. Demographically, they were at the stage which this country will reach some time after the year 2010 and, in addition, faced the current economic problems. They undertook a series of measures aimed at bringing in more revenue and containing costs. By 1981, two of the countries had eliminated the financial deficits, although only on a short-range basis. They are expecting an even more severe demographic problem later in this century and in the next. The measures in these two countries, as well as in most of the others, were not of a fundamental nature and were described by some commentators as "patchwork." There was no serious questioning of the social commitment to the programs, but only of the high level of costs involved.

ROLE OF PLANNING

Questions have been asked about the role which planning and economic projections had in this pattern. That is, did the planners fail or did they simply demonstrate that it may not be possible to plan long in advance? A view held in Europe is that long-range planning is not feasible and that is why the countries generally do not make projections far in advance.

This attitude is based on two factors: (1) The view that economic forecasts in the past assumed constant conditions and did not—and could not—take into account wars, the Great Depression, periods of extreme inflation, and demographic shifts; and (2) that new governments (administrations) are not obligated to follow the policies of their predecessors, they can and do make changes which cannot be predicted. For the shorter range, several of the countries (France and Germany) have "guideline" planning. Experience has shown that in drawing up plans for even 5 years, during the prosperous period before 1974, economists tended to warn of the necessity to think of the future demographic problems and to limit expansion, while the social and political pressures usually prevailed in favor of program improvements. Also, the shorter range projections usually reflected the current economic situation. Forecasts, even the demographic ones, tended to be more pessimistic during recession.

The plans and forecasts actually worked for a while and seemingly would have prepared the countries for the aging of the population, had it not been for the oil-induced recession since 1974. The basic problem since that time has not really been social security, but unemployment and the state of the economies. In order to solve the financial situation of the social security systems, it is necessary to bring about economic recovery.

LIMITS

"Is there a limit to the volume of social transfers?" This question, posed in a speech by the Director General of the ILO, was answered by him in the following way:

> While everyone would no doubt agree that there must be an absolute limit, this necessarily remains very imprecise and variable over time, so that it hardly seems possible to lay down a kind of "golden rule." * * * Nevertheless, it could be argued that in the * * * welfare states this proportion may now have almost reached a point where it is legitimate to begin talking about saturation.

He draws three main conclusions:

> The first is that social security benefits enjoy a privileged status within the context of public spending. Such benefits, far from being regarded as an item of expenditure and resented as a burden, are looked upon as a deliberate allocation of funds derived by the community as something worthwhile and reassuring.
>
> The second conclusion is that every country, as a result of the interplay of economic and social forces and to the extent

allowed by the resources placed at its disposal through the efforts of all its citizens, adopts a level of expenditure which differs, of course, from one country to another, but which corresponds to what is widely agreed at any particular moment to constitute the minimum standard of social protection.

The third conclusion is that, in view of the necessity of maintaining acquired social advantages when economic conditions are unfavorable, it is of vital importance to aim at greater efficiency in social security budgeting through a rationalization of the choices, structure, means, and services to be provided in the light of priority needs.

Before the oil recession, there was little if any awareness or discussion of a possible limit which a country could afford. Such discussion began as the systems went into deficit. The primary worry was not with old-age benefits, but with mounting health insurance costs, unemployment, and to some extent with rising disability insurance expenditures.

There is, then, no recognized maximum level of expenditures in any of the countries. In 1974, six of the eight countries devoted around 20 percent or more of GNP to all income security programs. By 1977, this spending had risen to more than 25 percent of GNP in five of the countries, 28 percent in the Netherlands, and 31 percent in Sweden. (The percentages probably continued to increase after 1977.)

Even with such high figures, however, several of the countries balanced their budgets, even if temporarily. Possibly only in Belgium are there serious problems, and that may be because of general economic conditions as well as the lack of a consensus on a series of revisions which successive governments have proposed.

There was also no general public concern about increases in the levels of payroll contributions. Employer organizations were the only groups to sound a warning about high "social costs" (contributions to all the programs, private pensions, and various kinds of fringe benefits). Perhaps the general public was not concerned because the payroll tax levels had gone up fairly gradually over the years and because the employer, in many instances, paid the larger potion.

The role and importance of a number of additional forces have not been discussed clearly, for example, the extensive use of foreign workers.

GUEST WORKERS

Can the decline in the labor force resulting from an aging population be offset by "importing" foreign workers? Beginning in the early 1960's, countries of Europe began to "import" workers, primarily from the Mediterranean countries—Italy, Greece, Yugoslavia, Turkey, Spain, etc. Also, within the European countries, workers can migrate from one country to another with virtually no restrictions. This movement was prompted by a shortage of labor, primarily because of the great economic expansion and also because of demographic distortions resulting from World War II.

Foreign workers were needed to meet the labor shortage and there was little, if any, thought of a potential impact on social security. Certainly there appears to be no evidence of planners thinking that guest workers would make up for the declining ratio of contributors to beneficiaries. International agreements were signed between the host country and the country of origin providing that guest workers would accrue credit toward eventual retirement benefits. When they retired, part of the benefit would be paid from the host country funds.

Attention was concentrated on the situation of the migrant workers and the retention of their rights when they returned to their own countries, and not on the impact which they might have on social security in the host countries. While almost nothing has been written about this aspect, it appears that the guest workers may have had a significant short-run effect on the demographic and financial developments of their host countries.

During a period in which the proportion of economically active workers was shrinking in Europe, the influx of the guest workers—6 million at the peak—made up in some measure for decreasing domestic labor forces. At the same time, the guest workers and their employers paid social security contributions in sufficient amounts to add appreciably to the total receipts of the national social security systems. Significantly, they would not be drawing benefits for years to come. During the period from 1957–77, the payouts in terms of old-age benefits were probably limited, since guest workers were normally hired at young ages and large numbers would not reach retirement until sometime in the 1990's or later.

IMPACT OF AGING POPULATION

Prior national discussions focused on unemployment, inflation, and other general economic conditions as being in large measure responsible for the deficits in social security. In other words, they focused on short-range economic problems. Except in Germany, the tendency was to avoid concentrating on the aging of the population as a primary factor in the social security deficits. Clearly, however, increases of up to 40 percent in the component of the population age 65 and over represented a benefit expenditure increase of approximately an equal amount. Now, concern over the demographic future has risen to major proportions.

INDEXING

How indexing has contributed to the rise of social security expenditures has not been brought out for those countries in which the benefit kept pace with the index on which it was based, or even lagged behind it.

Perhaps more significantly, the indexing procedures have in a number of cases not performed in the manner originally intended despite the actions of advisory committees which influence the amount of adjustment. The case of Germany can be cited as an example, since it has one of the most "elegant" indexing systems. The "dynamic" formula for adjusting benefits to changing economic conditions, which was introduced in 1957, was intended to act as a compensating mechanism that would dampen the effects of recession by increasing benefits, partially financed by reserves. New benefits were to be based on the average wage increases of 2½ and 3½ years before. The mechanism was expected to work in a countercyclical fashion, with the built-in lag expected to smooth out fluctuations. In hindsight, it appears to function well only with low inflation rates and high employment levels.

AGE OF RETIREMENT

Further study needs to be done on the impact of an earlier or flexible retirement age on the financing patterns of those countries which introduced such measures in the early 1970's.

FINAL OBSERVATIONS

From the perspective of the American observer, what are the most significant observations one can make about the European experience with social security?

First, the evolution abroad shows that European systems have been able to make adjustments for broad changes in the structure of their populations and in their economies.

Second, throughout this historical evolution, the commitment to social security has remained strong, so strong, in fact, that social security and income security programs have claimed a progressively larger share of GNP and higher payroll taxes.

Third, the successful evolution of the past has inspired a certain enduring confidence about the ability of the systems to deal with the problems of the future. Europeans seem to have developed the attitude that no matter what happens, social security will survive.

Fourth, the trend of expanding social security benefits in the 1960's and early 1970's followed by a period of short-term financing problems, is not unique to the United States. In fact, trends in the United States conform rather closely with the trends demonstrated abroad, even to the point of serious social security deficits in the aftermath of the oil crisis.

Fifth, the adjustments recently undertaken in Europe to deal with the short-term problem involved marginal changes which reduce the growth of benefits somewhat but preserve the essential features of the social security system. From an American standpoint, the major adjustments made abroad involved changes in the indexing of current benefits. It should be pointed out that such measures were widely debated on the national level before they were enacted. In the Federal Republic of Germany, for example, the placing of a cap on the indexing of benefits was preceded by several years of dispute and discussion involving the legislature, political parties, unions, employer organizations, social security advisory bodies, the general public, and the media. Prior to making such changes, there was a great deal of democratic disagreement before agreement could be reached on the specific measures.

Sixth, the European systems have no concrete, long-term plans to deal with the second cycle of an aging population—and the accompanying social security deficits—anticipated in the early decades of the 21st century. Traditionally, concern with the short-range prognosis has prevailed over the long-range forecasts, especially because foreign policymakers attach far less significance than do Americans to the forecasts of what the world will look like 75 years from now. Their experience has been that social security is not a program that is created and then left untouched for generations. Rather, social security is an institution for the benefit of society, which requires regular, if not constant, reappraisal, to insure that the system has sound financial balances and reflects society's expectations. Significantly, the debates abroad focus on ways of shoring up the financial problems through incremental changes, rather than through major reorganizations or wholesale benefit restructuring.

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