

# Social security finances

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## Introduction

One of the government's main functions is to protect the population against a number of social risks. Hence, replacement incomes are provided in the event of unemployment, old age, or occupational disability. In addition, income supplements are granted to compensate in part for the financial burden associated, in particular, with illness or with bringing up children. These social benefits are an important facet of the redistribution of income effected by the government.

In Belgium, social protection is provided mainly by the social security sub-sector. This is the largest component of the general government sector, so that it exerts a substantial influence on the evolution of public finances.

The first part of this article gives a general presentation of social security. It outlines the major developments in social security receipts and expenditure, and those concerning the social security financial balance and debt. The social benefits granted by other levels of government and by other European Union countries are also discussed. In particular, the effectiveness of social policies in combating poverty is judged against the results achieved by other countries. The second part of the article offers a more detailed analysis of social security receipts, presenting the pattern and structure of receipts together with the differences in funding methods between the system for employees and that for self-employed persons. The third part of this article focuses on social security expenditure. Apart from the structural changes observed in the past and the long-term projections for social benefits, this part also deals with the determinants of the main categories

of social security expenditure: health care, pensions, unemployment benefits, early retirement pensions, career breaks and reductions in working time and family allowances. Finally, the main conclusions are summarised.

## 1. Social security: general situation<sup>(2)</sup>

### 1.1 The main aggregates of the social security accounts: importance and trends

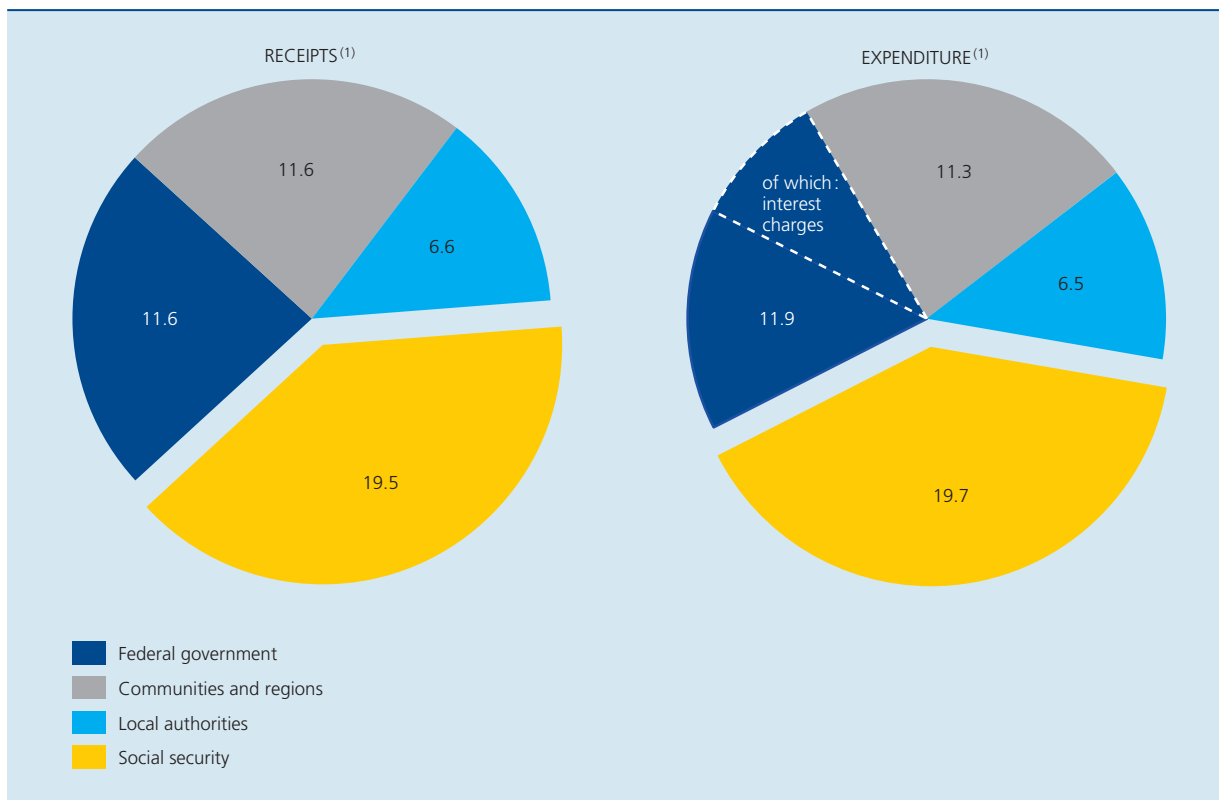
In 2004, social security receipts and expenditure (on a consolidated basis) totalled respectively 19.5 and 19.7 p.c. of GDP. Social security thus represented nearly 40 p.c. of all government receipts and expenditure, making it the largest sub-sector, ahead of the federal government and the sub-sector combining the communities and regions – which each accounted for just under a quarter of total receipts and expenditure – and the local authorities. Looking at primary expenditure only, i.e. expenditure excluding interest charges, social security even represented 44 p.c. of the total expenditure of general government.

However, the current level of social security receipts and expenditure is very different from what it was at the beginning of the 1970s, when the figures were 12 and 13 p.c. of GDP respectively. The rapid increase in unemployment, the growth of health care spending and the increases in certain benefits such as pensions,

(1) The authors wish to thank G. Langenus and H. Famerée for their comments.

(2) The figures relating to Belgian general government mentioned in this article are taken from the NAI's publication of the general government accounts dated 6 April 2005.

**CHART 1** RECEIPTS AND EXPENDITURE OF THE GENERAL GOVERNMENT SUB-SECTORS  
(percentages of GDP, 2004)



Sources: NAI, NBB.

(1) Receipts and expenditure are consolidated by deducting from the receipts and expenditure of each government sub-sector the transfers made to other sub-sectors. On a non-consolidated basis, the approach adopted for the rest of this article, social security receipts and expenditure totalled respectively 19.6 and 19.7 p.c. of GDP in 2004.

for example, contributed to the strong expansion of social security expenditure in the 1970s and early 1980s. In 1983, expenditure reached almost 22 p.c. of GDP. Receipts attained a similar level following measures to increase the contributions and the transfers from the federal government. The period of consolidation in the following years reduced the weight of social security to around 18 p.c. of GDP in 1990. Although budget discipline was relaxed for a short time in the early 1990s, that was soon followed by a further period of fiscal consolidation, partly related to the efforts to achieve the objectives required for joining the Economic and Monetary Union, so that, in 2000, social security receipts and expenditure had broadly returned to the same level as in the early 1990s. In the past few years they have resumed an upward trend.

Throughout the period from 1970 to 2004, social security receipts and expenditure moved very much in parallel. That parallelism is reflected in the minor fluctuations in the financial balance of social security, which ranged

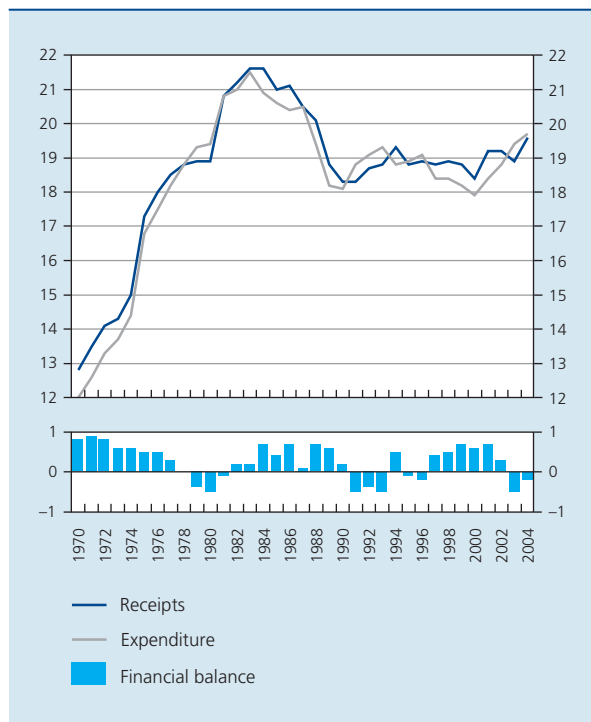
between a deficit of 0.5 p.c. of GDP and a surplus of 1 p.c. In 2004, the financial balance showed a small deficit of 0.1 p.c. of GDP.

As a result of this generally favourable evolution of the financial balance, the consolidated gross debt of social security has always remained relatively small. That debt peaked at 1.3 p.c. of GDP in 1995 and has since declined steadily. In 2001, the residual social security debt totalling 0.5 p.c. of GDP was taken over by the federal government in compensation for a reduction in the alternative funding<sup>(1)</sup>. Since then, social security has accumulated hardly any further debts.

Moreover, social security has a large portfolio of financial assets. The coexistence of debts and financial assets in the social security accounts is due partly to the fact that, before the introduction of "overall management"

(1) In regard to the scheme for employees, there was a single cut in the alternative funding in the same year; in the case of the scheme for self-employed persons, the cut was spread over several years.

**CHART 2** RECEIPTS, EXPENDITURE AND FINANCIAL BALANCE OF SOCIAL SECURITY  
(percentages of GDP)

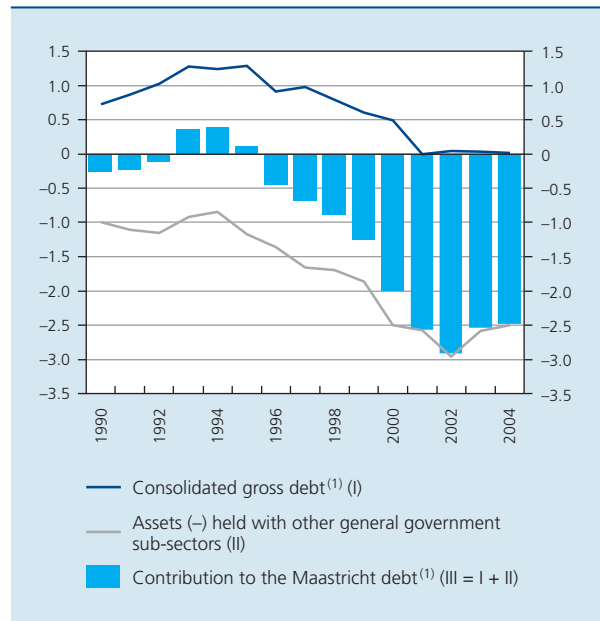


Sources: NAI, NBB.

in 1995, the various branches of social security were managed separately. Some branches had therefore accumulated a debt while others had regularly produced a budget surplus, and had therefore acquired a portfolio of assets. Insofar as these assets consist of government securities, they are deducted from the gross debt when calculating the debt figure used as a reference for the Maastricht Treaty criteria.

Since 1996, social security has contributed to the reduction in the level of the Maastricht debt. From 1996 to 2002 this favourable contribution showed a marked increase, on account of the budget surpluses achieved during that period and the corresponding increase in the volume of assets held on the other general government sub-sectors, which represented 2.9 p.c. of GDP in 2002. The deficits of the past two years, though small, have led to a reduction in the assets held by social security, so that the favourable contribution made by this sub-sector to the Maastricht debt declined to around 2.5 p.c. of GDP in 2004.

**CHART 3** SOCIAL SECURITY DEBT  
(percentages of GDP)



Sources: NAI, NBB.

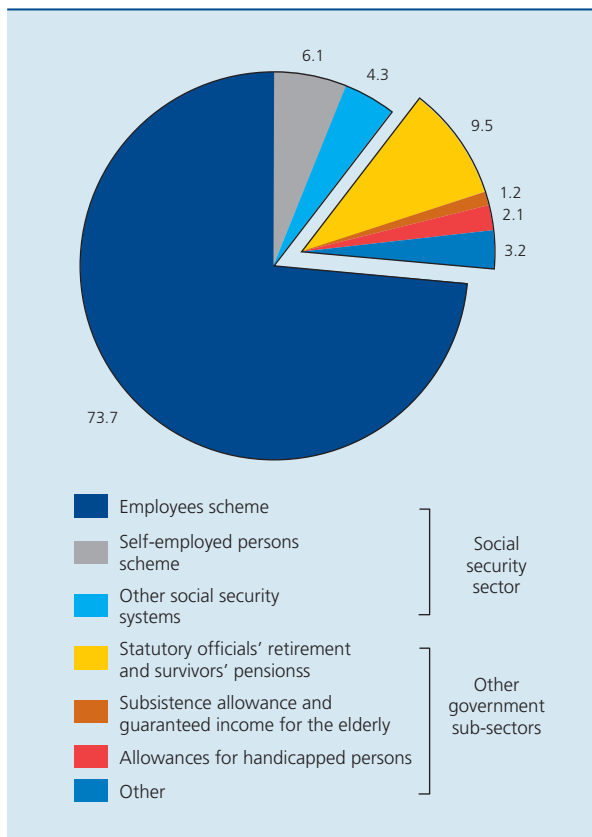
(1) The consolidated gross debt of social security is calculated by deducting the debts for which the counterparty is an institution in the same sub-sector (intra-sectoral consolidation). To obtain the latter's contribution to the Maastricht debt, the liabilities corresponding to an asset of another government sub-sector are deducted from the consolidated gross debt (inter-sectoral consolidation).

## 1.2 Social protection expenditure of general government

Not all the social provision made by the government is arranged through the social security sub-sector. Thus, the other levels of government generally pay their statutory officials' pensions and family allowances themselves. Furthermore, the federal government is responsible for paying allowances for handicapped persons, while the subsistence allowance is a social benefit paid by local authorities, though admittedly it is partly covered by federal government transfers. In 2004, social benefits which are not paid via social security made up 15.9 p.c. of the social benefits paid by general government. Retirement pensions and survivors' pensions of other government sub-sectors represented all of 9.5 percentage points.

Social security benefits, which accounted for 84.1 p.c. of total social provision in 2004, are paid mainly through the scheme for employees. In 2004, this scheme accounted for almost three-quarters of all social benefits, whereas the scheme for the self-employed represented 6.1 p.c. and the share of other – smaller – social security schemes, such as overseas social security, the provincial and local public service scheme, the subsistence funds,

**CHART 4** SOCIAL BENEFITS PAID BY GENERAL GOVERNMENT  
(percentages of the total, 2004)



Sources: NAI, NBB.

the Compensation Fund for workers made redundant as a result of business closure and the Vlaams Zorgfonds (Flemish Elderly Care Fund) came to 4.3 p.c.

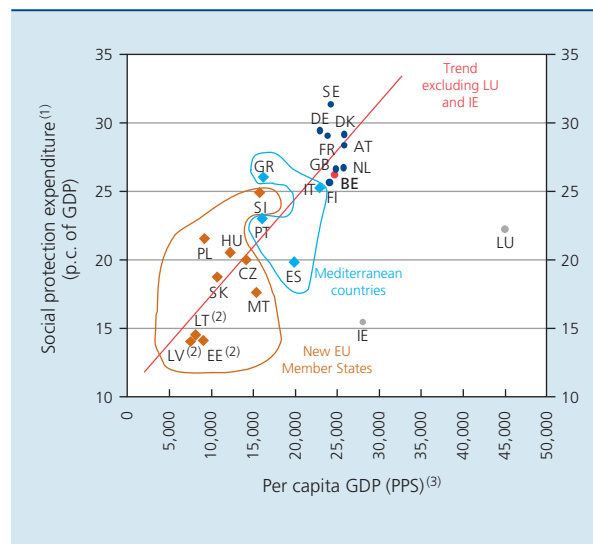
### 1.3 International comparison

International comparisons of social protection expenditure must be treated with caution. Some studies, such as those conducted by the European Commission (2004a), take account of not only public social protection expenditure but also mandatory private expenditure, consisting mainly of private health insurance and second pillar pensions. Conversely, the OECD (2004) limits the scope of the data to public expenditure in this area. A second point concerns the differences between countries in the way that social

protection is organised. Thus, while social protection expenditure mainly comes under social security in Belgium, that is not the case in all European countries. In Denmark, for example, social security pays only around 15 p.c. of social benefits, which are mainly the responsibility of the local authorities. It would therefore make no sense to consider social security expenditure only, and it is more appropriate to compare the social benefits paid by all public authorities together. Finally, the gross data used in international comparisons omit both the effect of taxation and parafiscal levies – which may weigh to a greater or lesser extent on the social benefits actually received by beneficiaries – and the effect of fiscal expenditure in the form of tax credits or other fiscal benefits. Nonetheless, some lessons may be drawn from international comparisons, which in this article relate to 2001 or 2002, the latest years for which data were available.

According to the OECD definition<sup>(1)</sup>, gross expenditure on social protection by all public authorities totalled 27.2 p.c. of GDP in Belgium in 2001; that was more than three percentage points higher than the EU-15 average. The level of public expenditure on social protection is highest in Denmark, where it totals 29.2 p.c. of GDP, and lowest in Ireland at 13.8 p.c. of GDP.

**CHART 5** SOCIAL PROTECTION EXPENDITURE<sup>(1)</sup> AND PER CAPITA GDP  
(2002, unless otherwise stated)



Sources: EC, NBB.

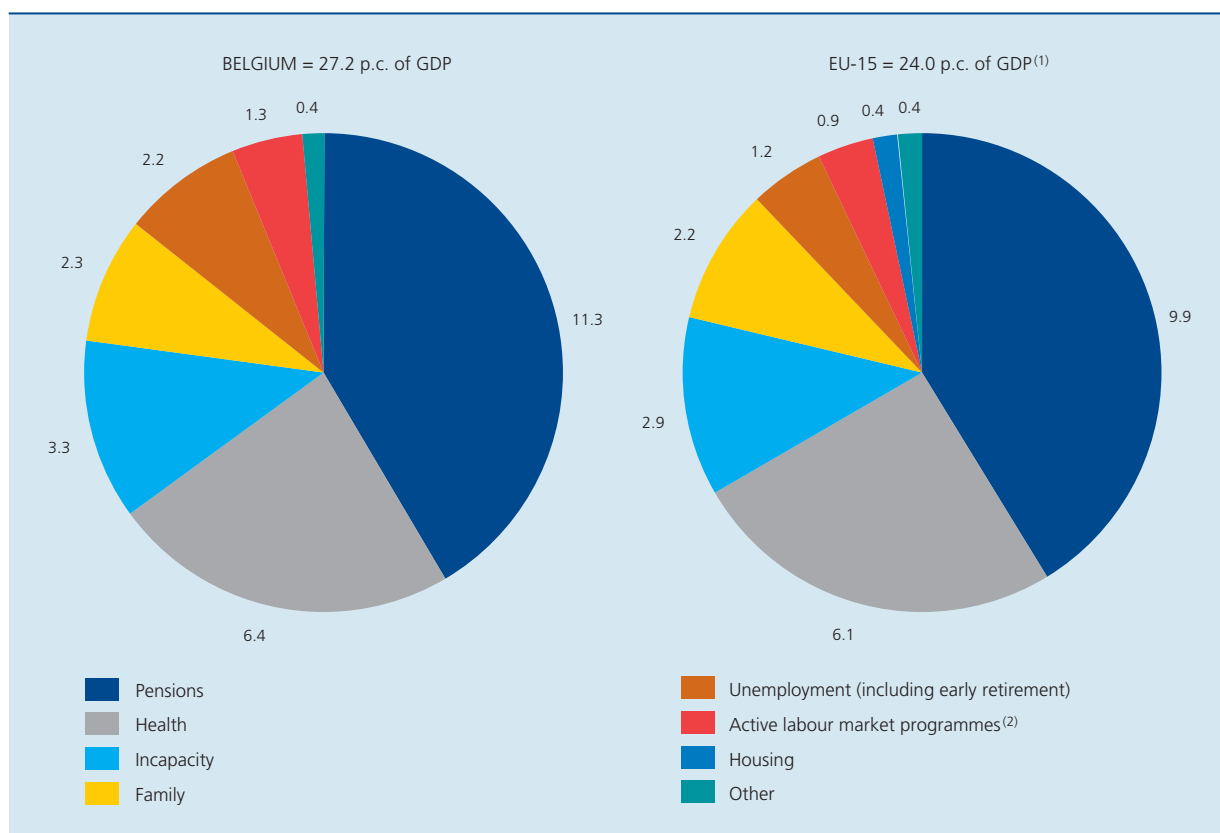
(1) Including mandatory private expenditure.

(2) 2001.

(3) Purchasing power standards (PPS) take account of the respective price levels in the Member States and of exchange rates.

(1) The definition of public social protection expenditure used by the OECD is broader than that used by the NAI in drawing up the national accounts. Among other things, it takes account of pensions paid by the Post Office and Belgacom, companies which – according to the national accounts methodology – do not belong to the government sector. In addition, certain social protection expenditure items are classified in different categories in the national accounts and according to the OECD methodology.

**CHART 6** SOCIAL PROTECTION EXPENDITURE OF GENERAL GOVERNMENT  
(percentages of GDP, 2001)



Source: OECD.

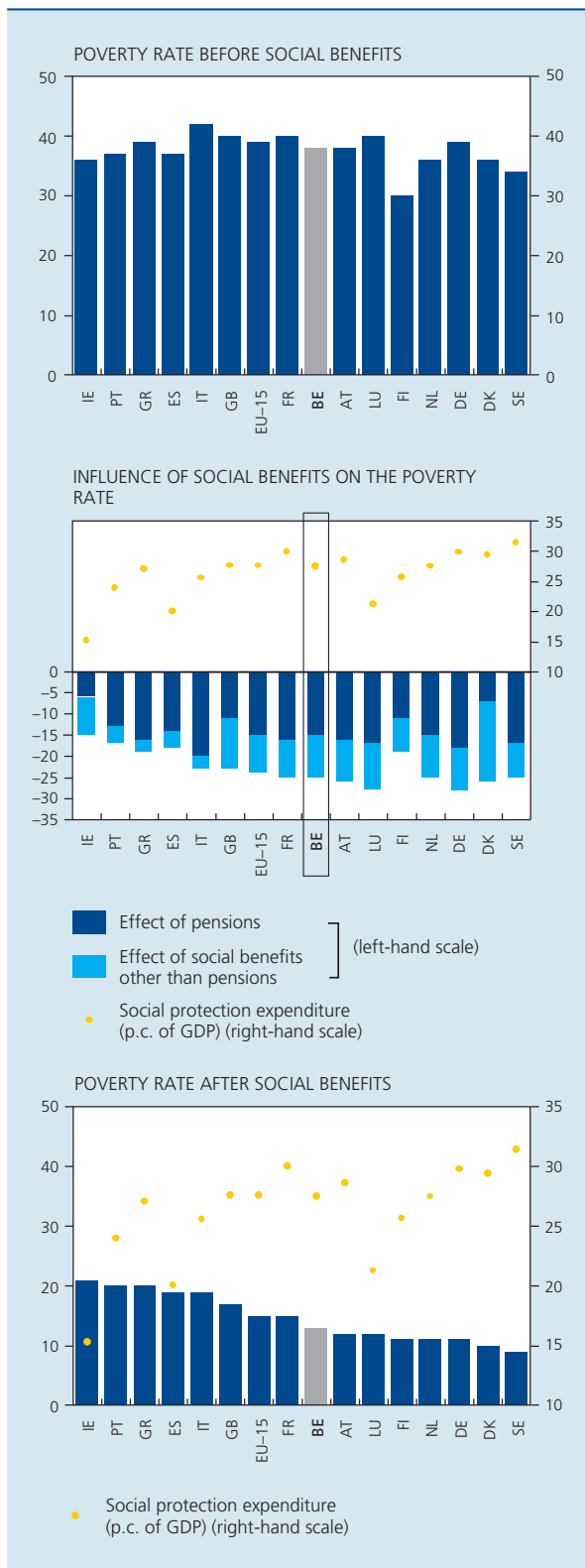
(1) Unweighted average.

(2) Including career break allowances and time credit.

The differences between Belgian public expenditure on social protection and the European average are due essentially to a few specific expenditure categories. Thus, public spending on pensions and unemployment in Belgium exceeded the European average by 1.3 and 1.1 percentage points respectively. The differences are much smaller for the other expenditure categories. For instance, public spending on health care in Belgium was hardly any higher than the EU-15 average in 2001. The same is true of public spending on incapacity and expenditure due to an active employment policy. The level of family allowances in Belgium was practically the same as in the EU-15. Finally, it should also be pointed out that Belgium does not have a structured system of housing allowances, since the social policy on housing is organised differently, whereas in the EU-15 housing allowances represented on average 0.4 p.c. of GDP in 2001.

There is a marked positive link between total social protection expenditure and per capita GDP. The EU countries can thus be divided into three groups. The new EU members have relatively low levels of prosperity and social protection. The Mediterranean countries (Italy, Greece, Portugal and Spain) form a second group comprising the lowest levels of per capita GDP and social protection expenditure in the EU-15. Finally, the social protection expenditure of the other Member States, which have a higher per capita GDP, varies between 25 and 31 p.c. of GDP. However, there are two notable exceptions to the link between the level of prosperity and public spending on social protection, namely Ireland and Luxembourg. In Luxembourg's case, that is probably due to the very high level of its GDP, whereas Ireland saw strong growth of its GDP in the 1990s and has a relatively young population.

**CHART 7** SOCIAL PROTECTION<sup>(1)</sup> AND POVERTY RATE<sup>(2)</sup>  
(2001)



Source : EC (2004a).

(1) Including the effect of mandatory private expenditure.

(2) Percentages of the population with an equivalent income below 60 p.c. of the median income.

#### 1.4 Effect of social benefits on the poverty rate

One of the main functions of social protection is to reduce poverty. The effectiveness of social benefits can be measured by the difference in the poverty rate, defined as the proportion of households with income below 60 p.c. of the median income, before and after intervention.

In a hypothetical situation with no social transfers, poverty rates in the EU-15 and in Belgium would have totalled 39 and 38 p.c. respectively in 2001. Taking account of pensions, the poverty rate falls to 24 p.c. in the EU-15 and 23 p.c. in Belgium. Social benefits other than pensions reduce the poverty rate by 9 and 10 percentage points respectively. In all, social benefits reduce the poverty rates as defined above to 15 p.c. in the EU-15 and 13 p.c. in Belgium.

The average figures for the EU-15 conceal wide variations between countries. The impact of pensions on the poverty rate is generally greater than that of other social benefits. However, it is only 6 percentage points in Ireland, whereas the figure for Italy is 20 points. Denmark records the highest impact of social benefits other than pensions on the poverty rate (19 percentage points), while the lowest impact is recorded in Italy and Greece (3 percentage points).

The poverty rate ranges from 9 p.c. in Sweden to 21 p.c. in Ireland. If the poverty rate is compared with social protection expenditure as a percentage of GDP, a significant link becomes apparent between these two indicators: the higher the social protection expenditure in proportion to GDP, the lower a country's poverty rate.

## 2. Social security receipts

Social security receipts can be divided into a number of categories. First there are the social contributions – namely employers' and employees' contributions and the contributions of self-employed persons and non-active persons – which make up the bulk of social security receipts<sup>(1)</sup>. Next there are the transfers from other government sub-sectors, particularly the federal government<sup>(2)</sup>. These transfers consist partly of grants and partly of funding based on the sharing of the tax revenues collected by the Treasury, defined in the official jargon as

(1) The special contribution for social security is included in the social contributions here, whereas in the government accounts it is regarded as own tax revenue of the social security system.

(2) Since 2001, there has also been a transfer from the Flemish Community to the Vlaams Zorgfonds, which is part of the social security sub-sector in the government accounts.

**TABLE 1** SOCIAL SECURITY RECEIPTS  
(percentages of GDP)

	1970	1980	1990	2000	2004
1. Social contributions .....	9.4	11.7	13.8	13.8	13.7
Employers' .....	6.1	7.6	8.9	8.4	8.2
Employees' .....	2.6	3.0	3.9	4.3	4.4
Self-employed .....	0.7	0.9	0.8	0.9	0.8
Non-active .....	0.1	0.1	0.2	0.3	0.3
2. Transfers from other government sub-sectors .....	2.8	6.7	4.0	4.0	5.2
Grants .....	2.8	6.5	3.8	2.5	2.5
Alternative funding .....	0.0	0.1	0.2	1.5	2.8
3. Own direct and indirect taxes .....	0.0	0.1	0.2	0.4	0.5
4. Non-fiscal and non-parafiscal receipts .....	0.5	0.5	0.4	0.2	0.1
Total .....	12.8	18.9	18.3	18.4	19.6

Sources: NAI, NBB.

alternative funding. Finally, social security also has its own tax revenues as well as limited non-fiscal and non-parafiscal receipts.

### 2.1 Trend in receipts and changes in their composition

Social security receipts have expanded significantly in recent decades, rising from 12.8 p.c. of GDP in 1970 to 19.6 p.c. in 2004. Most of that growth took place in the 1970s and the early 1980s. In 1984, these receipts even peaked at 21.6 p.c. of GDP. During the ensuing period they subsided, dropping to 18.3 p.c. in 1990. Thus, as already mentioned, they followed a pattern very similar to that of expenditure.

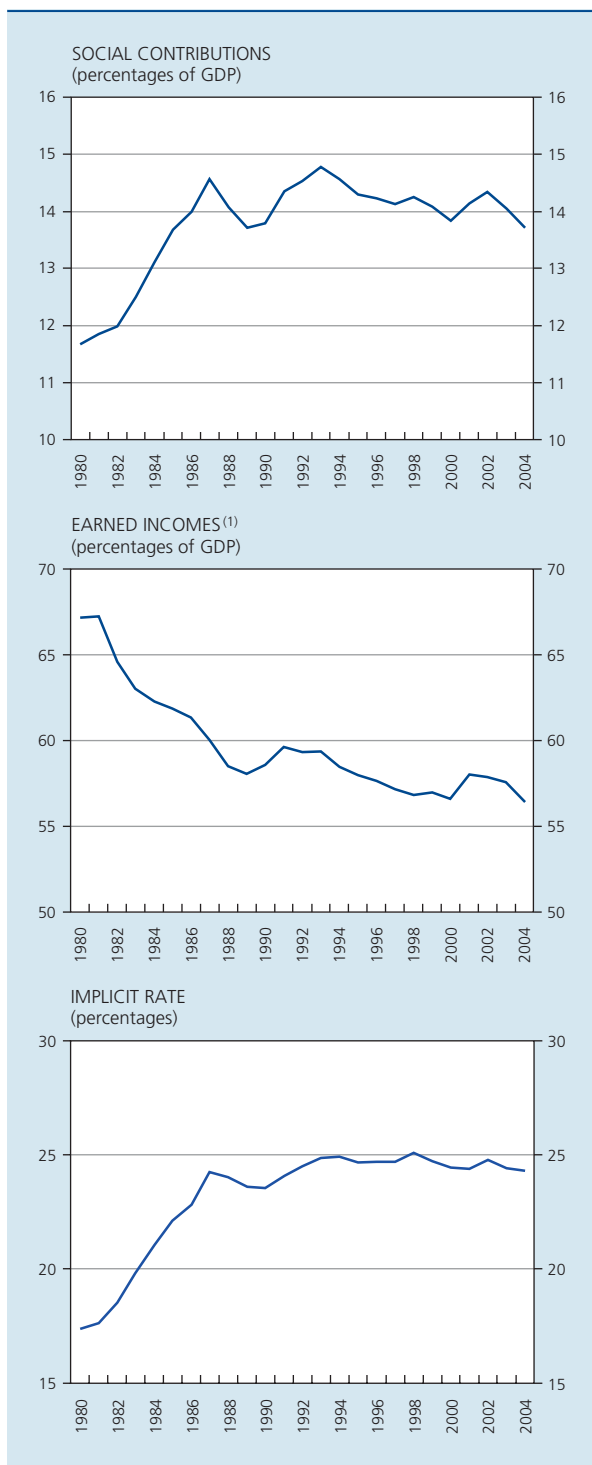
At first, the strong expansion of social security was financed mainly by larger grants from the federal government. However, in view of the worsening budget deficits, the federal government made substantial cuts in these transfers during the 1980s. Social contributions gradually increased by just over two percentage points of GDP during each of these two decades as various measures were introduced. As a result, the social security funding structure – the relative share of the various categories of receipts – was more or less the same in 1990 as in 1970.

After 1990, receipts fluctuated around 18 to 19 p.c. of GDP. The funding structure also remained virtually unchanged. However, the federal government decided that it would progressively replace funding in the form of grants with alternative funding. In 2004 there was a substantial rise in the alternative funding of social security, totalling 1.1 p.c. of GDP, not only in order to guarantee the financial balance of social security, but also – at a rate of 0.4 percentage point – to cover the transfer to social security of the part of the daily cost of hospitalisation which had previously been paid by the federal government. Following this change, the share of social contributions in social security receipts declined to 70 p.c. in 2004.

### 2.2 Social contributions

As already stated, social contributions are the main source of funding for social security. They increased from 9.4 p.c. of GDP in 1970 to 11.7 p.c. in 1980, then to 13.8 p.c. in 1990. In 2004, they totalled 13.7 p.c. This growth was due partly to the rise in earned incomes – which form the main basis of the contributions – as a percentage of GDP, and partly to the rise in the implicit rate (i.e. the ratio between the social contributions levied and earned incomes). Since these data are only available from 1980 onwards, the detailed analysis of social contributions is confined to that period.

**CHART 8** SOCIAL CONTRIBUTIONS



Sources: NAI, NBB.

(1) Earned incomes comprise the remuneration of employees and the gross mixed income of self-employed persons, excluding imputed social contributions.

Despite the steep fall in earned incomes as a percentage of GDP, down from 67.2 p.c. of GDP in 1980 to 58.6 p.c. in 1990, social contributions expressed as a percentage of GDP increased considerably during that period. This rise is therefore attributable solely to the marked increase in the implicit rate, which went up from 17.4 p.c. in 1980 to 24.3 p.c. in 1987, and remained more or less steady at 24 to 25 p.c. in the ensuing period. This considerable increase in the parafiscal burden on labour is due to various measures taken in the framework of the consolidation of public finances.

Thus, October 1982 saw the abolition of the remaining wage ceilings for contributions to certain branches of the scheme for employees<sup>(1)</sup>. Furthermore, the concept of remuneration was extended to include, in particular, the double holiday allowance. The main reason for the increase in employers' contributions was the introduction of wage moderation contributions corresponding to the cancelled indexations in 1984, 1985 and 1987. The rate of employees' contributions for private sector workers went up from 9.07 p.c. in 1980 to 12.07 p.c. in 1987. In addition, a contribution payable by single persons and households without children and a levy on family allowances were introduced. In 1992, these two contributions were abolished, but the rate of employees' contributions was raised to 13.07 p.c. For the self-employed, contribution rates were increased and the maximum levels of income to which these rates applied were raised; a moderation contribution corresponding to the pay moderation of employees was also imposed on self-employed persons. Similarly, there was a sharp rise in contributions from non-active persons, owing to the introduction of various new contributions such as the solidarity levy on statutory pensions, disability allowances and early retirement pensions. Finally, in 1994 the special contribution for social security came into force.

Conversely, the reductions of employers' contributions curbed the growth of social contributions. These reductions were introduced in order to restrain labour costs, particularly for new employees taken on, and – in the beginning – especially for industrial firms exposed to foreign competition, as part of the so-called Maribel operation. In 1999, these reductions in employers' contributions, together with the reductions in charges for the low paid, were converted into a structural reduction which was subsequently extended. In 2004, the various reductions in employers' contributions were simplified

(1) Until 1994, social contributions under the scheme for employees were divided among the various branches of social security, in line with the percentages fixed by law. A "Social security financial balance fund" received special levies and contributions and transferred the proceeds to the branches for which the allocated contributions were insufficient. Since 1995, however, the bulk of the contributions and transfers from the federal government have been placed under the "overall management" system which finances the various social security branches according to their needs.



and harmonised. On that occasion, the majority of the existing specific rules were replaced by an overall reduction in employers' contributions, composed of two elements: first, the structural reduction mentioned above, which varies according to the worker's pay, and second, a number of reductions for target groups, in favour of older workers, the long-term unemployed, first jobs, young workers and the collective reduction in working time. In addition, a special reduction was granted for workers who were made redundant by restructuring and have found a new job through a job centre.

In the framework of the Employment Conference in 2003, it was decided to continue extending the reductions in contributions. In addition, the "work bonus" which incorporates the tax credit for the low paid in the reduction in employees' social security contributions on the lowest wages – introduced on 1 January 2000 – came into effect in 2005. The amount of the work bonus declines only gradually as earned income increases, so as to provide an incentive to work more or to seek a better paid job.

### 2.3 Other social security receipts

In 2004, other social security receipts represented just under one-third of total receipts. Around 27 p.c. of the total consists of transfers from other government sub-sectors. They primarily concern federal government funding in the form of grants and alternative funding. This last form of finance is considered partly as compensation for the loss of receipts in terms of social contributions, caused by the reductions granted to employers and workers.

In addition, social security has its own direct and indirect taxes, which represented 2.6 p.c. of its total receipts in 2004. These specific taxes include levies on various insurance products, a levy on the turnover of the pharmaceutical industry, specific payments by insurance companies to the Industrial Accidents Fund and the annual lump-sum contribution payable by companies in favour of the scheme for self-employed persons, introduced to take account of the fact that the activities of the self-employed are increasingly pursued in the form of a company.

Finally, social security also collects a small amount of non-fiscal and non-parafiscal receipts, such as interest paid on its financial assets.

(1) However, the self-employed receive a temporary allowance in the case of bankruptcy.

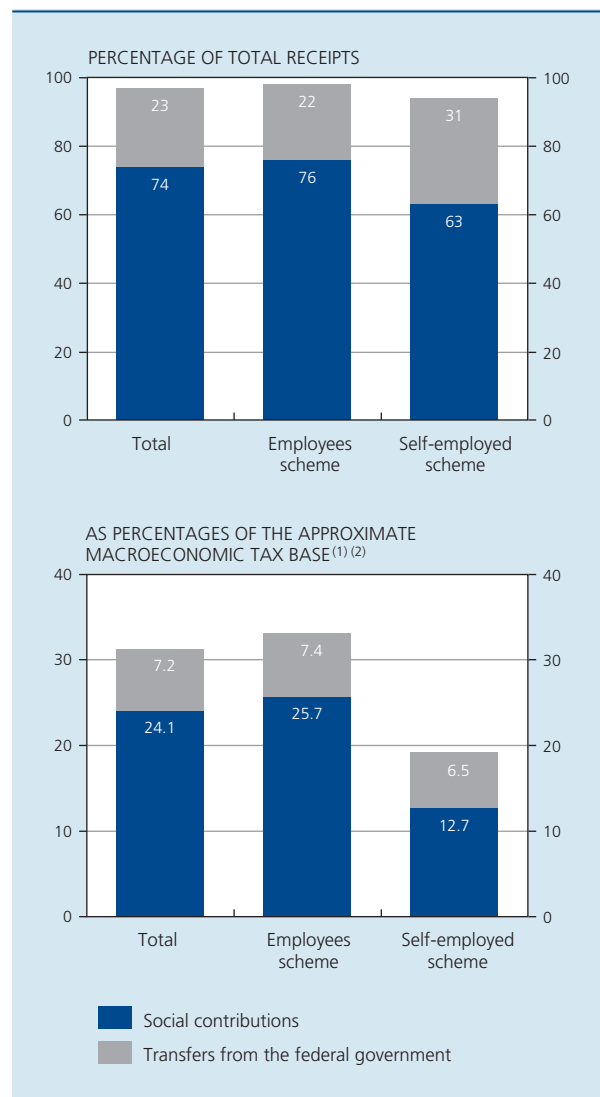
(2) Mandatory insurance against minor health risks for the self-employed is to be introduced in July 2006.

### 2.4 Comparison of the funding of the scheme for employees and the scheme for self-employed persons

The self-employed are not covered by social security to the same extent as employees. They therefore have to pay lower contributions. Thus, self-employed workers are not insured against unemployment,<sup>(1)</sup> nor against minor health risks,<sup>(2)</sup> and their pensions are lower.

**CHART 9** FUNDING OF THE SCHEME FOR EMPLOYEES AND THE SCHEME FOR SELF-EMPLOYED PERSONS

(2003)



Sources: NAI, NBB.

(1) For employees, this is the wage bill less imputed contributions. For the self-employed, it is net mixed income.

(2) These results should be interpreted with caution since the macroeconomic variables used do not entirely correspond to the tax base of the contributions. The rate of contributions payable by employees in the private sector is currently 13.07 p.c., whereas the rate of employers' contributions in this sector is at least 33.03 p.c. In 2005, the rate of social contributions from the self-employed came to 19.65 p.c. on a maximum income of 45,604 euros (with a minimum of 459 euros per quarter), 14.16 p.c. on the second slice of income up to 67,301 euros and 0 p.c. on any excess.

There are major differences in the structure of receipts in both schemes. The self-employed persons' scheme obtains relatively less receipts from social contributions and more from federal government transfers. In 2003, social contributions represented 63 p.c. of receipts in the scheme for self-employed persons – excluding the annual lump-sum contribution from companies – against 76 p.c. in the employees' scheme. Federal government transfers accounted for 31 p.c. in the scheme for self-employed persons, against 22 p.c. in the employees' scheme.

In the self-employed persons' scheme, the implicit contribution rate, i.e. the ratio between the contributions and the most appropriate possible macroeconomic measurement of the tax base, represents only half of that in the employees' scheme. In relation to this macroeconomic measurement of income, federal government transfers are slightly smaller in the self-employed persons' scheme than in the employees' scheme.

### 3. Social security expenditure

Having explained the main sources of finance for social security, it is important to examine the uses to which these funds are assigned. This section first presents an overall profile of social security expenditure in the past and the structural changes which have taken place, together with a very brief account of the prospects for the future. It then focuses on the main categories of expenditure individually, describing their development and that of their determinants.

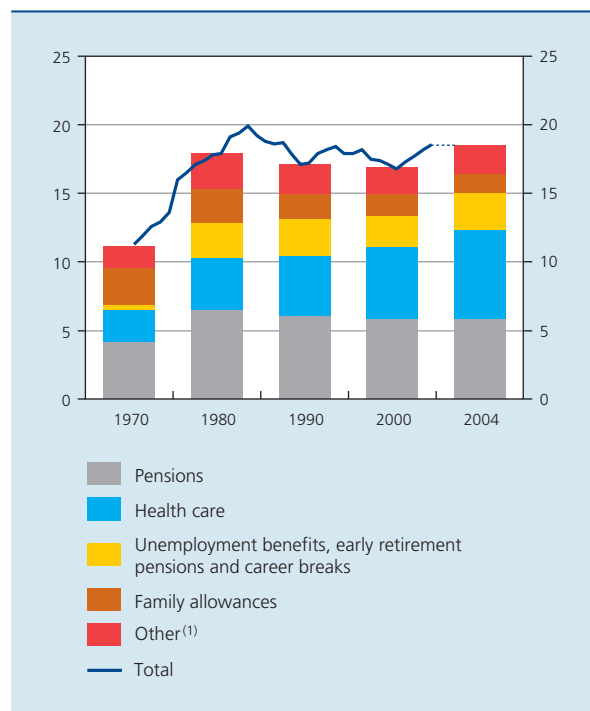
Social security benefits represent around 95 p.c. of the sub-sector's total expenditure. The other expenditure of social security, such as compensation of social security employees, current purchases of goods and services or business subsidies,<sup>(1)</sup> which represent only just over 1 p.c. of GDP, will be disregarded in the rest of this chapter. Therefore, the term "expenditure" in this article will refer only, somewhat imprecisely, to social benefits.

#### 3.1 Trend in expenditure and changes in its composition

Social security expenditure grew from 11.3 to 18.6 p.c. of GDP between 1970 and 2004, an increase of 7.3 percentage points of GDP. This period can be divided into five phases, defined by the years of peaks and troughs in total expenditure expressed as percentages of GDP.

(1) This mainly concerns the social Maribel for the non-profit sector. From the point of view of the national accounts, this is regarded as a business subsidy, even though it is applied by way of a reduction in social contributions.

**CHART 10** SOCIAL BENEFITS PROVIDED BY SOCIAL SECURITY  
(percentages of GDP)



Sources: NAI, NBB.

(1) Mainly sickness/disability allowances and social benefits from the subsistence allowance funds, including the Compensation Fund for workers made redundant by business closures.

In the 1970s and up to 1983, expenditure rose steeply, increasing from 11.3 to 19.9 p.c. of GDP, an all-time high. This strong growth is mainly attributable to unemployment benefits which expanded at a very rapid rate, averaging almost 18 p.c. per annum over this period as a whole in real terms. Although the growth of the other expenditure items was more moderate, the rate of expansion was still higher – at 5.5 p.c. – than it ever has been since. This other expenditure therefore also contributed to the scale of the increase, primarily as a result of pensions being adjusted in line with prosperity and the increase in health care spending.

The decline in social security expenditure, totalling 2.8 points of GDP between 1983 and 1989, is due to the reduction, in real terms, in unemployment benefits, family allowances and sickness and disability benefits, and to the limited increase in expenditure on pensions. The period 1989-1993 saw an increase in social benefits amounting to 1.2 percentage points of GDP. Apart from the rapid rise in expenditure on health care and pensions, this increase was also due to higher expenditure on unemployment benefits. As a result of the budgetary consolidation,

**TABLE 2** SOCIAL BENEFITS PROVIDED BY SOCIAL SECURITY(averages of the percentage annual change at constant prices,<sup>(1)</sup> unless otherwise stated)

	1970-1983	1983-1989	1989-1993	1993-2000	2000-2004
Unemployment benefits .....	17.8	-2.5	5.6	-1.2	5.9
Other social benefits .....	5.5	1.2	3.2	1.5	3.7
of which:					
Pensions .....	6.0	1.2	3.0	1.2	1.5
Health care <sup>(2)</sup> .....	6.1	3.7	5.8	3.1	5.0
Other .....	4.6	-0.6	1.0	0.3	2.4
<i>p.m. GDP at constant prices</i> .....	2.3	2.7	1.4	2.8	1.4
<i>p.m. Social benefits as p.c. of GDP<sup>(3)</sup></i> .....	8.6	-2.8	1.2	-1.5	1.7

Sources: NAI, NBB.

(1) Expenditure deflated by the national consumer price index.

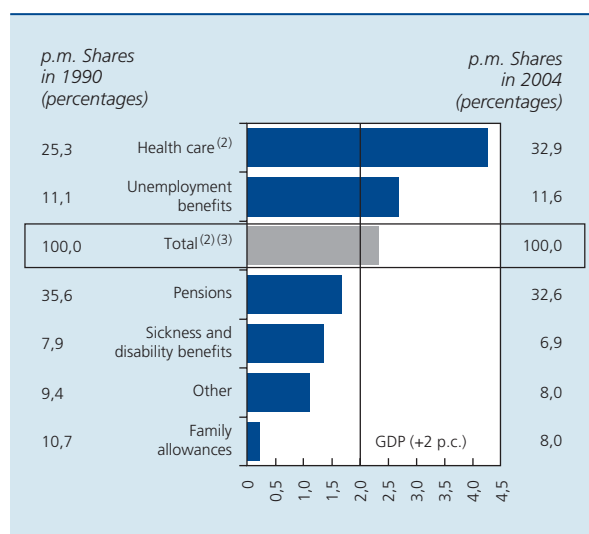
(2) Adjusted for the effect on expenditure of the transfer to social security, in 2004, of the part of the daily cost of hospitalisation which had previously been paid by the federal government.

(3) Total change between beginning and end of period.

due partly to the pursuit of the objectives required for joining the Economic and Monetary Union, the level of social benefits in 2000 was 1.5 percentage points of GDP below that of 1993. Over the period 1993-2000, all categories of social security expenditure contributed to the decline, except for health care. Finally, between 2000 and 2004 the return to strong growth of social security expenditure, which increased by 1.7 percentage points of GDP,<sup>(1)</sup> was due mainly to a rapid increase in health care expenditure and rising unemployment.

These developments are therefore attributable to cyclical factors, which mainly affect the movement in unemployment benefits, and structural factors, which influence the amount of pensions paid, for example, as well as to decisions relating to the government's fiscal policy, which may be more or less expansionary or restrictive. However, during the five phases identified above, growth appears to speed up and slow down simultaneously for all the main expenditure categories. Viewed overall, social security expenditure appears to be counter-cyclical, as the strong growth of expenditure occurs at the time of a slowdown in GDP growth, and vice versa.

Taking the period 1970-2004 as a whole, the growth of social benefits is due mainly to the rapid rise in health care expenditure, which amounted to 6.4 p.c. of GDP in 2004 against only 2.4 p.c. in 1970. Expenditure relating

**CHART 11** SOCIAL SECURITY EXPENDITURE CATEGORIES(average annual percentage change from 1990 to 2004, at constant prices,<sup>(1)</sup> unless otherwise stated)

Sources: NAI, NBB.

(1) Expenditure deflated by the national consumer price index.

(2) Adjusted for the effect on expenditure of the transfer to social security, in 2004, of the part of the daily cost of hospitalisation previously paid by the federal government. As a result of the transfer of this expenditure to social security, the share of health care in total social benefits provided by social security increased from 32.9 to 34.6 p.c.

(3) Benefits paid by the Vlaams Zorgfonds, which represented 0.4 p.c. of total social benefits in 2004, are not included.

(1) This growth takes account of the effect on expenditure of the transfer to social security, in 2004, of the part of the daily cost of hospitalisation previously paid by the federal government. After adjustment for this item, the increase in social benefits between 2000 and 2004 came to just 1.3 percentage points.

to the labour market – unemployment, early retirement pensions and career breaks – also contributed to this growth, namely at a rate of 2.3 percentage points of GDP, and so did pensions which increased from 4.1 to 5.9 p.c. of GDP over the period considered. In contrast, family allowances contracted, falling from 2.7 to 1.4 p.c. of GDP. Other social benefits taken as a whole increased by 0.5 percentage point of GDP.

If the analysis is confined to a more recent period, namely 1990-2004, social security expenditure has grown at an annual average of 2.3 p.c. in real terms, outpacing the growth of GDP. Health care is still the fastest growing expenditure item, up by an annual average of 4.3 p.c. Unemployment benefits have also increased faster than GDP and total social expenditure. Expenditure on pensions and sickness and disability benefits has increased, but more slowly than GDP and total social expenditure. Finally, in 2004 family allowances were hardly any higher

than their 1990 level in real terms. As regards the “other” categories, this chapter will return later to the particularly marked changes in expenditure on career breaks and reductions in working time, and to the relative decline in early retirement pensions. It should also be noted that benefits in respect of occupational diseases have declined, following changes in the structure of the economy and the nature of work.

The share of health care in total social expenditure thus increased from a quarter in 1990 to a third in 2004. For the first time, this item thus represented a higher share than pensions which, although declining in relative terms, still represent almost one-third of social benefits. All other social benefits together also account for around one-third of social security expenditure, the main components being unemployment benefits, family allowances and sickness and disability benefits.

### Box – Projection of social expenditure up to 2030

The Study Group on Ageing, set up under the High Council of Finance, is responsible for estimating the long-term consequences of population ageing in Belgium. In its latest annual report, dated May 2005, the Study Group assumes a GDP growth rate at constant prices averaging 1.9 p.c. per annum (2004-2030), on the basis of average annual increases in labour productivity and employment of 1.7 and 0.2 p.c. respectively. However, this expansion of employment, which should raise the employment rate by around 6 percentage points by 2030, requires continuation of an active policy, notably to reduce the level of structural unemployment.

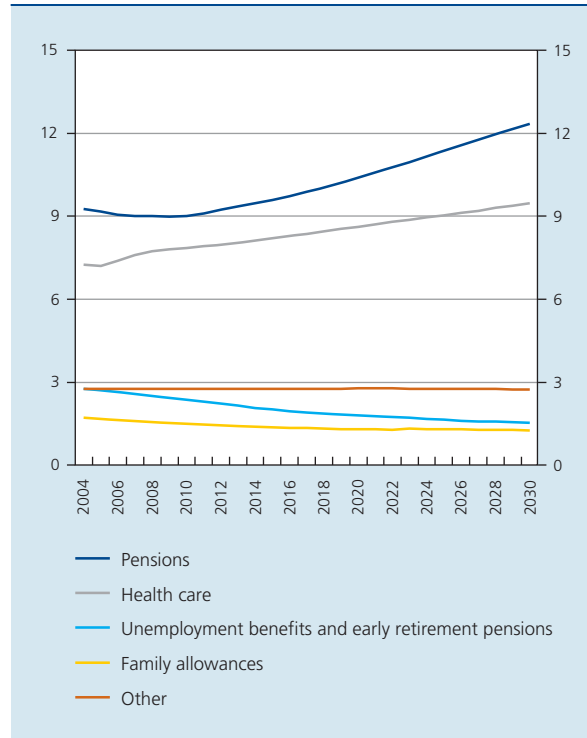
Making these and other assumptions, such as an adjustment of social benefits to rising prosperity averaging 0.5 p.c. per annum, and a health expenditure growth rate of 4.5 p.c. per annum in real terms up to 2007<sup>(1)</sup> later dropping to an average of 2.8 p.c. between 2008 and 2030, the Study Group on Ageing estimates the cost of ageing – defined as the net rise in social expenditure – at 3.6 percentage points of GDP between 2004 and 2030. The cost of pensions is expected to increase by 3.1 percentage points of GDP over this period. Within this category, the pensions of employees are projected to increase by 2.4 percentage points of GDP, while those of public officials will rise by just 0.7 percentage point of GDP. The share of self-employed persons' pensions is expected to remain unchanged. The expansion of health care, the second largest increase, is estimated to total 2.3 percentage points of GDP. Conversely, other social benefits will probably attenuate the cost of ageing to some extent: unemployment benefits and early retirement pensions should decline by 1.2 percentage points overall and family allowances should fall by 0.4 percentage point of GDP between now and 2030.

(1) Excluding the impact of the mandatory insurance, planned for July 2006, against minor health risks for the self-employed.



REFERENCE SCENARIO FOR THE TREND IN SOCIAL EXPENDITURE<sup>(1)</sup>  
 BETWEEN NOW AND 2030

(percentages of GDP)



Source : Study Group on Ageing.

(1) The Study Group on Ageing deals with the social expenditure of general government, so that the levels of the various expenditure categories and their total differ from the figures used in the rest of this article, which focuses on the social security sector.

### 3.2 Expenditure categories : developments and determinants

Apart from the general developments described, each expenditure category is influenced by a number of specific factors. These factors consist of the number of recipients of a type of benefit and the average amount of the benefit received by each one. This last determinant is calculated implicitly for each of the categories except for health care spending for which this analysis is less appropriate.

#### 3.2.1 Health care

As indicated before, health care is currently the largest social security expenditure item. Moreover, its relative size is steadily increasing, since the average rate of growth – 3.7 p.c. between 1980 and 2004 – is the highest of all expenditure categories.

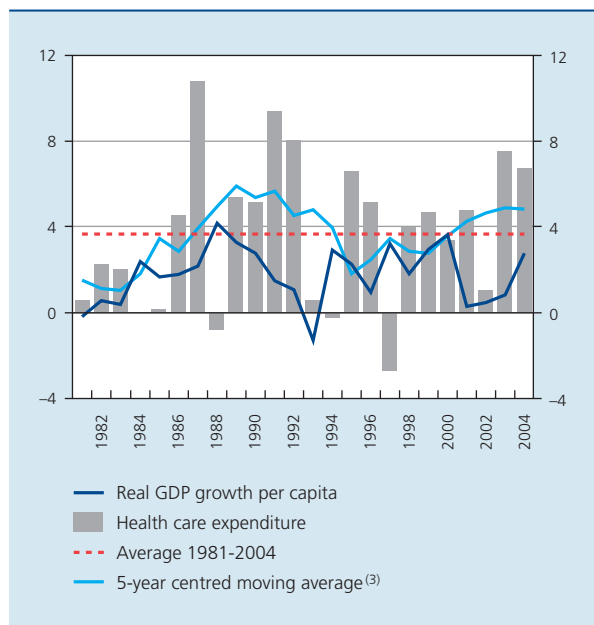
However, the real growth of health care expenditure is highly volatile. It has been negative in some years, but particularly large in others. The use of a centred moving average makes it possible to smooth out these annual fluctuations to some extent, particularly by eliminating shifts from one year to the next – due partly to accounting delays – and short-term measures.

In the first half of the 1980s, health care expenditure grew at a moderate pace. Subsequently, and up to the beginning of the 1990s, growth was particularly rapid. However, this period was followed by a phase of below-average growth. In the past few years, the growth of health care expenditure has been well above the trend rate. It was particularly pronounced in 2003 and 2004, at rates of 7.5 and 6.7 p.c. respectively in real terms. The setting of a 4.5 p.c. growth norm, as under the July 2003 coalition agreement, was therefore

CHART 12

HEALTH CARE EXPENDITURE<sup>(1)</sup>

(percentage change at constant prices compared to the previous year<sup>(2)</sup>)



Sources: NAI, NBB.

- (1) Public expenditure on health care, excluding sickness and invalidity benefits, expenditure on long-term care insurance, transfers to institutions caring for the handicapped, and disability benefits, but including the part of the hospital charge per day which was paid by the federal government until 2003.
- (2) Expenditure deflated by the national consumer price index.
- (3) Real growth was assumed to be 4.5 p.c. in 2005 and 2006 for the purpose of calculating the moving average for 2003 and 2004.

insufficient to contain expenditure within the planned budget.

Demographic factors account for 0.8 percentage point of the increase in health care expenditure, which averaged 3.7 p.c. from 1980 to 2004. The population expanded by an annual average of 0.3 p.c., while the effect of ageing, determined by the changing population structure and the average expenditure per age group, came to 0.5 percentage point. Overall, it is therefore estimated that non-demographic factors contributed 2.9 percentage points to the average annual increase in health care expenditure.

These last factors comprise multiple elements, such as medical and technological progress, the fact that prices tend to rise faster in the health care sector, which is relatively labour-intensive, changes in behaviour on the demand side – particularly because of the increased supply of health care and the higher standard of living – and the impact of various measures aimed at improving access to health care.

The Study Group on Ageing assumed that health care expenditure would grow by an annual average of 3 p.c. between 2004 and 2030 in real terms. During that period, population ageing would still be a key factor in the growth of expenditure: its impact on the annual expansion of health care was estimated at 0.7 percentage point, whereas population growth was expected to account for 0.2 percentage point.

The impact of non-demographic factors is, by its nature, difficult to predict, so that the projections on this subject are particularly difficult. Most of the projection methods used in relation to health care, including the one used by the Study Group on Ageing, establish a link between these non-demographic factors and the rise in per capita GDP. Thus, the expansion of health care expenditure should decelerate progressively on account of the expected slow-down in per capita GDP growth, owing to the decline in employment from 2015, taking account of the predicted long-term demographic trends.

3.2.2 Pensions

Pension expenditure grew in real terms by an annual average of 1.7 p.c. between 1990 and 2004. This growth was particularly strong in the early 1990s, peaking at 4.1 p.c. in 1991, and was again above average in 2002 and 2003. The two determinants of the total amount of pensions contributed to this growth: on average over this period, the number of pensioners increased by 0.8 p.c. per annum and the amount of the average pension, calculated implicitly, rose by 0.9 p.c. per annum at constant prices.

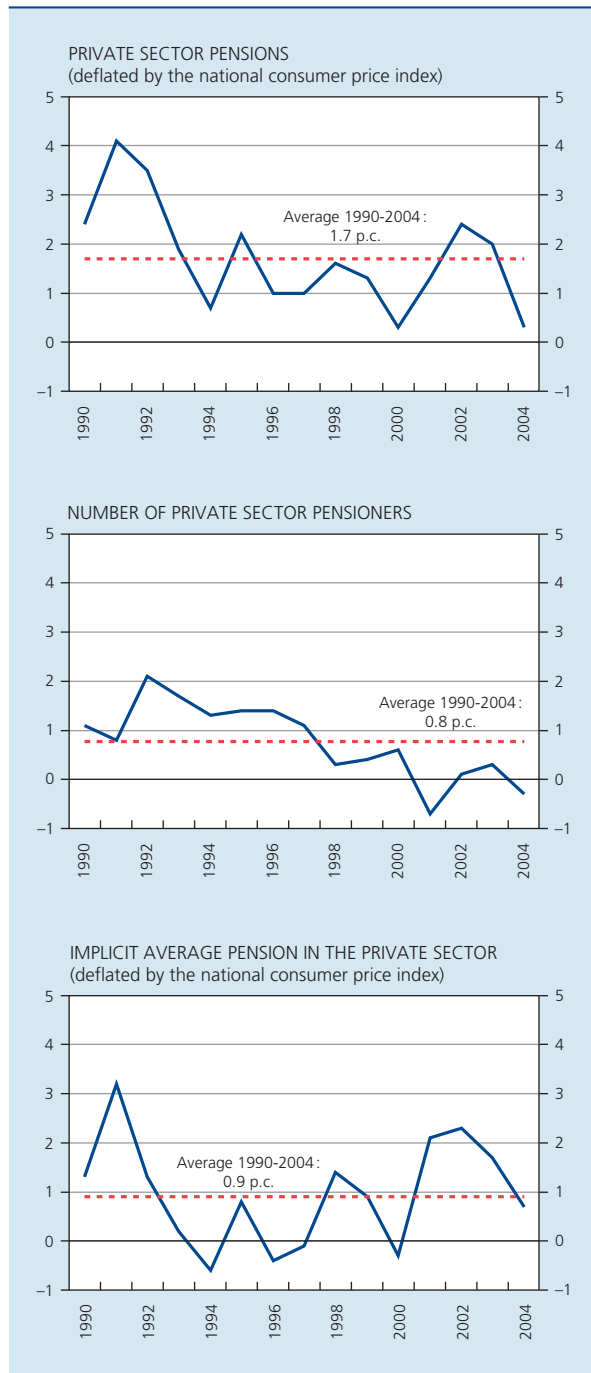
3.2.2.1 Number of beneficiaries

There are three main schemes for pensioners: employees and the self-employed come under the private sector pension system, while statutory public officials come under the public sector pension system. The latter are therefore outside the scope of social security expenditure since their pensions are paid directly by the other public authorities<sup>(1)</sup>.

Altogether, the number of private sector pensioners increased from around 1.6 million in 1990 to roughly 1.7 million in 2004, a rise of 11 p.c. Growth was relatively sustained until 1997, then slowed down markedly and was actually negative in 2001 and 2004. This trend reversal was due at least partly to changes in the law, as the pension scheme for employees and the self-employed

(1) However, some of the officials employed by local authorities (provinces and municipalities) come under the social security pension system if the authority employing them has opted to contribute to the NSSOPLA.

**CHART 13** SOCIAL SECURITY PENSION EXPENDITURE AND DETERMINANTS  
(percentage change compared to the previous year)



Sources: NAI, NPO, NBB.

was reformed by the Framework Law of 26 July 1996. This reform gradually increases both the statutory retirement age for women and the denominator of the fraction of working years used to calculate their pension, thus encouraging them to work longer. In addition, the employment history conditions which must be met in

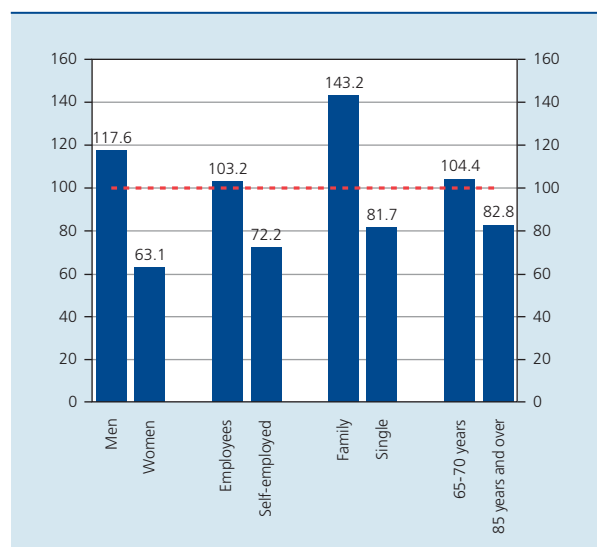
order to qualify for early retirement from the age of 60 are being progressively tightened up for both men and women.

In its projections, the Study Group on Ageing estimates that the number of beneficiaries under the schemes for employees and the self-employed should increase by 59 and 30 p.c. respectively between now and 2030. While this increase is expected to be fairly limited until 2010, it will subsequently accelerate. This strong rise in the number of pensioners is the main factor determining the predicted increase in pension expenditure of the social security system.

3.2.2.2 Average real implicit amount of pensions

In all, the growth of average implicit pensions at constant prices came to 13.7 p.c. between 1990 and 2004. Although this growth tended to see-saw, it is nonetheless possible to identify certain trends. Thus, growth was fairly rapid at the beginning of the 1990s, boosted mainly by the increases granted to the oldest pensioners. Since 2001 it has again been fairly rapid, similarly as a result of measures in favour of the lowest and the oldest pensions. Between these two periods of rapid growth, the average amount of a pension remained more or less unchanged, mainly because no welfare adjustment was granted between 1991 and 1999.

**CHART 14** AVERAGE AMOUNTS OF SOCIAL SECURITY PENSIONS<sup>(1)</sup>  
(2004, sample average index = 100)



Sources: NPO, NBB.

(1) Sample restricted to persons over 65 years old, "pure" employees or self-employed excluding combination careers, without taking account of survivors' pensions or guaranteed income schemes.



There are still large differences between the average amounts of pensions received by the various categories of pensioners. On average, women receive a gross pension which is only half that of men, because their working life is generally shorter and their pay is lower on average. The pensions of the self-employed are 30 p.c. lower than those of employees, on average. Single persons receive only about 60 p.c. of the amount applicable for “family” pensions. Finally, “young” pensioners aged from 65 to 70 years receive pensions which are 25 p.c. higher than those of persons aged 85 years and over, the reason being the upward trend in wages, which form the basis for calculating the pensions, and the fact that existing pensions are only partially adjusted in line with prosperity.

These differences, combined with changes in the structure of the retired population, have had an impact on the movement in average pensions at constant prices, an impact which is likely to persist, at least to some extent. The increase in the female participation rate and the decline of the amount of “family” pensions, which is an indirect consequence of that, depress the amount of the average pension. The rise in the percentage of the oldest pensioners is another factor curbing the average pension amounts. The replacement of “older pensioners” with “young pensioners” exerts the opposite effect, as does the reduction in the proportion of the self-employed.

Finally, in recent years discretionary measures have mainly concerned adjustment of the oldest pensions in line with prosperity and increases of the lowest pensions. These measures, which – as announced by government announcement – are to continue in the years ahead, have generally had a positive impact on the average amount of pensions.

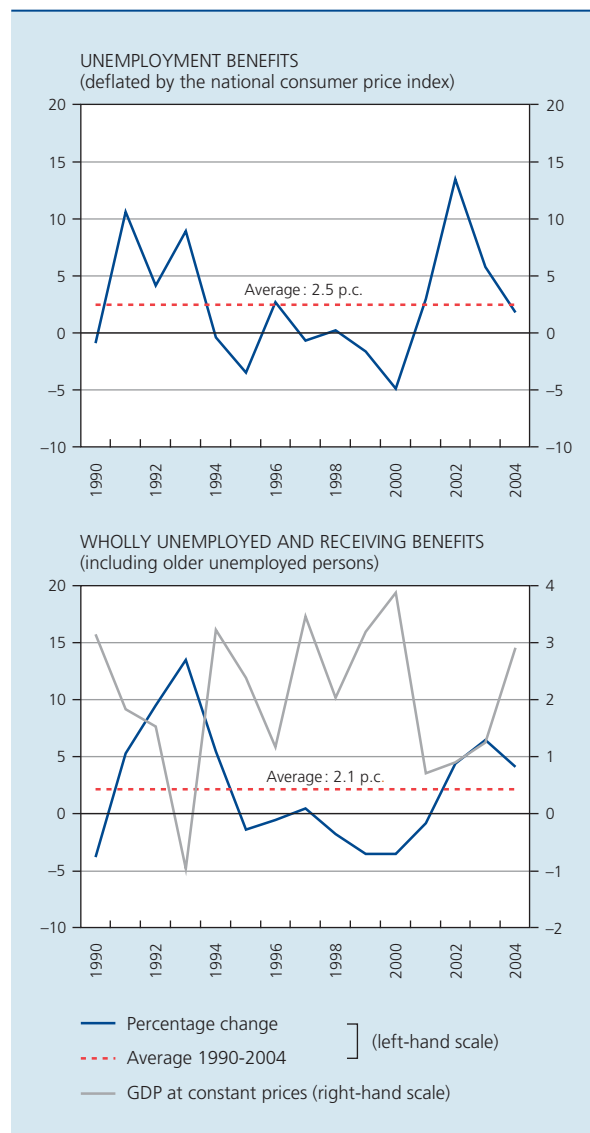
### 3.2.3 Expenditure relating to the labour market

Expenditure relating to the labour market falls into three categories: unemployment benefits, early retirement pensions and schemes for career breaks and reductions in working time. They are sometimes grouped together, as NEMO is the institution paying these benefits. However, treating them separately, as it is done here, makes it possible to analyse the trends and determinants in greater detail.

#### 3.2.3.1 Unemployment benefits

Unemployment expenditure increased in real terms by an annual average of 2.5 p.c. between 1990 and 2004. This growth was fairly strong in the early 1990s and again between 2001 and 2003. Conversely, the total amount

**CHART 15** UNEMPLOYMENT EXPENDITURE AND NUMBER OF UNEMPLOYED  
(percentage change compared to the previous year)



Sources: NAI, NEMO, NBB.

of unemployment benefits declined overall between 1994 and 2000.

Over the period as a whole, this increase was due almost exclusively to the rise in the number of unemployed<sup>(1)</sup>, at an annual average of 2.1 p.c. Apart from an upward trend which will not be discussed here, the movement in the number of unemployed is greatly influenced by the business cycle. Thus, unemployment grew fairly rapidly between 1991 and 1994 and from 2002 onwards,

(1) This group was restricted here to persons wholly unemployed and receiving benefits, including the older unemployed, since they receive the great majority of the unemployment benefits.



owing to the marked slowdown in activity during those periods. Conversely, from 1995 to 2001, the number of unemployed fell almost every year.

The average amount of the benefits, calculated implicitly, grew by only 0.3 p.c. per annum in real terms over the 1990-2004 period as a whole.

3.2.3.2 Early retirement pensions

In contrast to unemployment benefits, expenditure on early retirement pensions has declined since 1990, by an annual average of 1.4 p.c. in real terms. The only periods in which these benefits increased were the years 1990-1992 and 2003-2004. The medium-term evolution is due mainly to the reduction in the number of early retired, down by 1.5 p.c. per annum over the period as a whole,

while there has been practically no change, on average, in the implicit benefits since 1990.

The link between the economic cycle and the number of early retired is less marked than in the case of unemployment. That difference is probably due to the method of departure from each system: exits from the unemployment scheme are at least partly linked to the business cycle, whereas exits from the early retirement pension scheme are determined by the age attained by persons who have taken early retirement, and their switch to pensioner status. It is therefore only the movement in the number of new persons taking early retirement that is subject to cyclical variations. This factor also probably explains the unusual rise in the number of early retired in 2003 and 2004. The generally buoyant economy of the second half of the 1990s had in fact produced relatively fewer persons taking early retirement than before. As a result, at the time when these relatively small cohorts reached the statutory retirement age, exits from early retirement status were fewer in number. Combined with a slowdown in activity in recent years, this factor is probably contributing to restoring positive growth in the numbers taking early retirement.

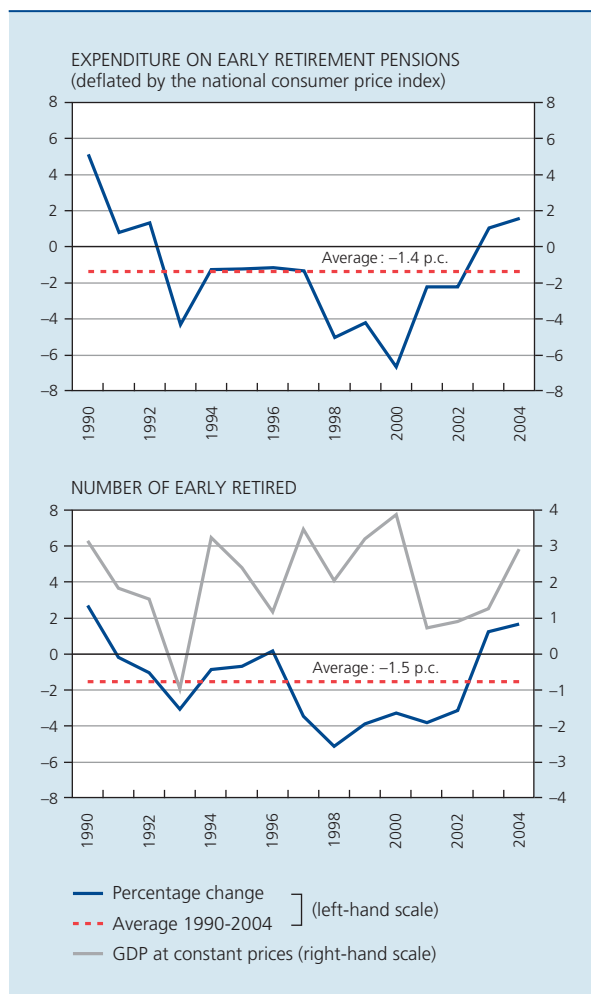
Another point worth mentioning is that growth of around 1.5 p.c. in the number of early retired, as in 2003 and 2004, corresponds to an average increase of just over 1,500 persons, so that factors of a more microeconomic nature may also play a part in this trend.

3.2.3.3 Career breaks and reductions in working time

Although this was the category of social security expenditure which saw the strongest growth, the weight of career breaks and reductions in working time is still very small, at less than 0.2 p.c. of GDP. The real annual average growth of 10.3 p.c. since 1990 is due almost entirely to the increase in the number of persons participating in these schemes, averaging 10.1 p.c. per annum, so that the number practically quadrupled over the period as a whole.

The rise in the number of people receiving benefits for career breaks and reductions in working time is due to the wide range of formulas offered to workers. Thus, on the one hand there has been the gradual development of time credit schemes (full or part time), 4/5 working time, reductions in working time for workers aged 50 years and over, and on the other hand special schemes such as parental leave, carer's leave and medical treatment leave.

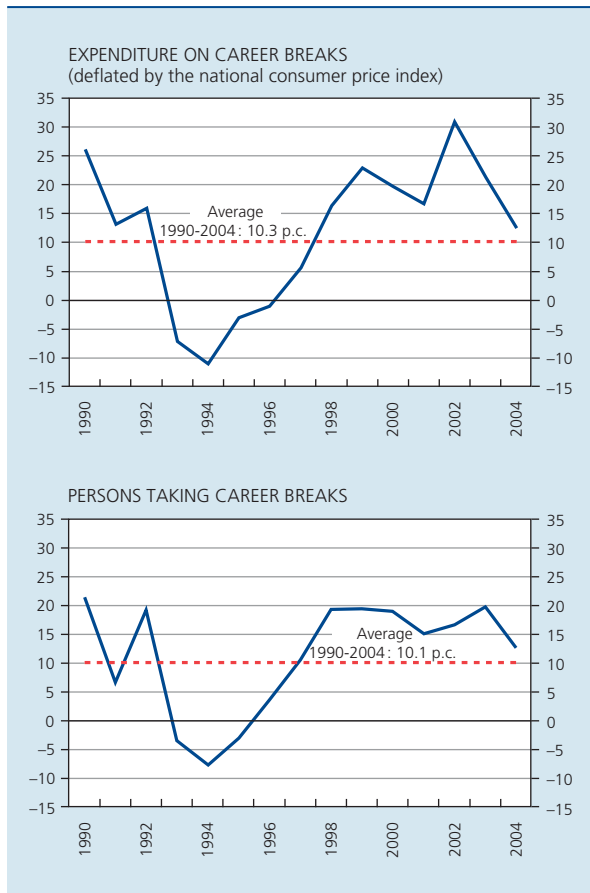
**CHART 16** EXPENDITURE ON EARLY RETIREMENT PENSIONS AND NUMBERS TAKING EARLY RETIREMENT  
(percentage change compared to the previous year)



Sources: NAI, NEMO, NBB.

**CHART 17** EXPENDITURE ON CAREER BREAKS AND REDUCTIONS IN WORKING TIME, AND NUMBER OF PERSONS CONCERNED

(percentage change compared to the previous year)



Sources: NAI, NEMO, NBB.

Although these measures were introduced at a specific moment, their success is dependent on a change of attitude. It is therefore likely that their influence will make itself felt gradually, so that sustained growth will probably last.

### 3.2.4 Family allowances

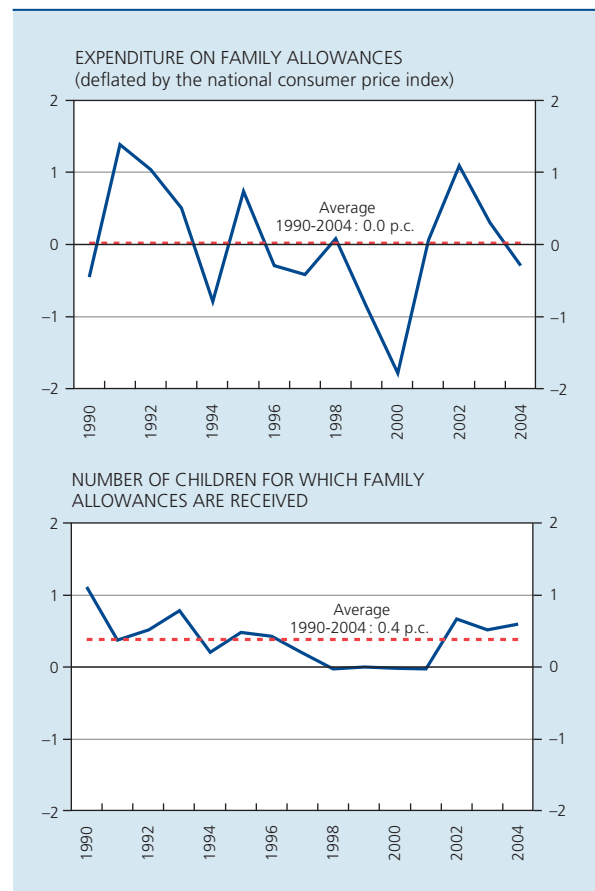
In 2004, expenditure on family allowances was practically the same, at constant prices, as it was in 1990. This relative stabilisation is due to a small rise in the number of beneficiaries, averaging 0.4 p.c. per annum, while the average amount paid per qualifying child declined in the same proportion at constant prices. In 2004, these benefits represented 1.7 p.c. of GDP, compared to 2.1 p.c. in 1990.

The rise in the number of beneficiaries recorded since 1990, which exceeded population growth, is due to various factors. Thus, some beneficiaries who had previously come under specific systems (employees of Belgacom, the Post Office and the RTBF) were gradually incorporated in the private sector system of family allowances. In addition, the trend towards staying in education for longer means that the allowances are paid out over a longer period. The recent acceleration in growth, which has averaged 0.6 p.c. since 2002, is due partly to the weakness of the economy, as young job seekers retain their entitlement to family allowances during the waiting period (for unemployment benefits) immediately following completion of their education.

The decline in the average amount of the family allowances appears to be due mainly to the reduction in the number of children per family, as the amount of the allowances depends on the child's rank and increases for each additional child.

**CHART 18** SOCIAL SECURITY EXPENDITURE ON FAMILY ALLOWANCES AND NUMBER OF QUALIFYING CHILDREN

(percentage change compared to the previous year)



Sources: NAI, NOFA, NBB.

## 4. Conclusions

On the basis of the above analysis, a number of conclusions can be drawn.

First, it has been shown that the level of social benefits paid by the government in Belgium, essentially via the social security sector, is higher than the European average. This difference is due mainly to relatively higher expenditure on pensions and unemployment.

In addition, the analysis illustrated the fact that social security expanded particularly strongly in the 1970s. In the ensuing period, total receipts and expenditure remained relatively stable on average; expressed as percentages of GDP, they stood in 2000 at roughly the same level as in 1980. During this period, however, there was a “stop and go” policy on expenditure and receipts, in that the expansion periods were followed by periods

in which a restrictive policy was pursued. In recent years, social security has again been expanding, although only to a limited extent. The analysis also showed that the structure of social security expenditure has undergone profound changes, resulting partly from a strong rise in health care expenditure.

Since receipts and expenditure have hitherto moved very much in parallel, the financial balance of social security has always hovered around equilibrium. At present, the social security sector is not only free of any financial liabilities, it actually has substantial financial assets.

Finally, population ageing will clearly exert strong upward pressure on future expenditure on pensions and health care. This increase can be only partly offset by the predicted decline in unemployment expenditure and family allowances. Therefore, social security will have to face a major financial challenge in the (near) future.

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