

# MPRA

Munich Personal RePEc Archive

## **An Incomes Policy for the Professions: the Dutch Experience**

v an der Hoek, M.

Erasmus University Rotterdam

January 1988

Online at <http://mpra.ub.uni-muenchen.de/6120/>

MPRA Paper No. 6120, posted 05. December 2007 / 15:42

# An Incomes Policy for the Professions: the Dutch Experience

By M. PETER VAN DER HOEK\*

**ABSTRACT.** In 1951 the United States began moving toward an *incomes policy*, an attempt to end postwar wage and price *inflation* by linking changes in these prices to gains in *productivity*. Other countries later followed suit; some countries had already adopted wage and price control policies. The *Netherlands* moved toward an incomes policy immediately after World War II. Initially, the Dutch program involved *wages* only, but in the 1970s it became an accepted principle that private *professional income* should be comparable with the salaries of *government officials* and *civil servants* with comparable training and responsibilities. In the Netherlands (as in the United States and, before *medicine* was socialized, the United Kingdom) *health professionals* operate on a fee-for-service basis and their incomes escalated as a result of both inflation and monopoly power. So they were subjected to the incomes policy. The policy's effectiveness in curbing income escalation cannot be determined with certainty—reliable data are lacking. However, the evidence indicates that the policy failed to achieve its original purpose.

## I

### Introduction

WHILE THE POSTWAR INCOMES POLICY of the Netherlands has drawn international attention, judgments about its effectiveness differ widely. Whereas one author considers the policy to have been useful and beneficial,<sup>1</sup> others regard it as a failure.<sup>2</sup> Concerning the effectiveness of the British incomes policy there are varying views as well.<sup>3</sup> In the United States the incomes policy was abandoned as ineffectual in favor of counter-inflationary monetary policies as well as measures to control the demand, such as health maintenance organizations staffed by salaried and contractual professionals.

These divergent opinions mark the problem of evaluating an incomes policy: one can make use of different criteria, depending on the purpose(s) of the policy. Although price stability or stability of labor costs might be an objective

\* [M. Peter van der Hoek, is associate professor of economics, Erasmus University, Room H16-24, P.O. Box 1738, 3000 DR Rotterdam, The Netherlands.] An earlier version of this paper was presented on April 18, 1986 at the 21st Atlantic Economic Conference in St. Thomas, U.S. Virgin Islands. The author gratefully acknowledges the helpful comments of Bob Haveman on earlier drafts of this paper.

of an incomes policy, other goals are possible as well. A more equitable payments structure, for instance, or improving the structure of payments systems in bargaining processes are examples.<sup>4</sup>

In this study I do not deal with the Dutch incomes policy as a whole, but instead with only one aspect of it. In an international context, the Dutch incomes policy contains a unique feature with reference to policy for professional remuneration. This is an almost completely neglected subject in the English language literature about the Dutch incomes policy and labor relations.<sup>5</sup>

The Dutch government seeks to subject the professions<sup>6</sup> to an incomes policy for two primary reasons. First, in Dutch politics it is a widely accepted opinion that an incomes policy should be a comprehensive one: all incomes should be involved. Second, the existence of State regulated entry to the professions gives those professions market power and implies the need for State regulation of income. Especially because of the latter, the Dutch incomes policy concerning the professions can be seen as a case study of the struggle between private interests and the general public interest.<sup>7</sup>

The first attempts to develop an incomes policy for the professions in the Netherlands came at the end of 1971. Since that time, regular consultations have been held between the Dutch government and representatives of the professional bodies. The government emphasized the need to develop a coherent and integrated incomes policy and the desirability of more public understanding about the labor element of professional earnings.<sup>8</sup> In 1974 these consultations resulted in the publication of a report, drafted by a working group,<sup>9</sup> pointing out that there are three main differences between wage earners and the self-employed: (1) a difference in legal status (2) a difference in socioeconomic position and (3) a difference in pension rights. The working group recommended an investigation or inquiry into the 1972 incomes of the professions.

The consultations with the professional bodies about the way to carry out this inquiry did not progress smoothly. On the contrary, so many questions were raised that the inquiry forms could not be sent out until 1977. The consultations about the presentation of the results of the inquiry progressed equally laboriously, so that the results could not be published until 1981. Meanwhile the 1972 data had become obsolete and the inquiry's results were no longer relevant to an incomes policy for 1981 and later. Thus the value of the inquiry should be sought in its methodology.

In this study the current state of affairs concerning the Dutch incomes policy for the professions is examined. First, I shall present an inventory of the barriers to entry for the professions, because these barriers to entry—or (more generally) regulations—are one of the primary reasons for government intervention. Second, I shall focus on the "acceptable income level" and its separate elements.

Finally, I shall discuss the policy the government has pursued concerning the incomes of the professions.

## II

### **Regulations Governing Entry to the Professions**

IN 1975 THE DUTCH GOVERNMENT published a note about the incomes policy containing a brief review of the remuneration structure of the professions. It stated that in pursuing an incomes policy for the professions, it should obviously consider the fee representing the value of the labor services provided. This would be in connection with (and follow naturally from) the more general wage policy being pursued. Furthermore the Government stated that the integration of the professions into a comprehensive incomes policy is hindered by a lack of concrete information about fees and sufficient data concerning the level, the growth and the spread of the professional incomes. This integration is also hampered by the protected market positions of the professions brought about by the entry barriers. Moreover, and related to entry barriers, the Government considers the policy of the professions to accept or not to accept a patient or a client to be a distortion of normal market structure.<sup>10</sup>

The control of entry exercised by the professions is in fact a restriction upon entry. Two elements compose this barrier. Generally, the occupational training forms a high threshold for potential entrants, the more so as the number of training facilities (especially for certain professions in the health care sector) is limited. Moreover, there are more or less formal regulations in force concerning the requirements for establishing production facilities. In the following I shall review briefly these regulations for each professional category.

The most rigorous establishment regulations refer to *public notaries*, an occupation devoted to providing stated legal services. In this matter the professional group plays an important role, although the final word in regard to the admission of candidates to the ranks of the public notaries rests with the Minister of Justice. This official decides upon the succession of and change in the number of posts. Referring to the real estate part of the services of public notaries, price competition is ruled out through uniform fees,<sup>11</sup> whereas for other documents minimum fees are in force. By far the greatest part of the notary services is dictated by law and reserved to public notaries. Third party competition comes only from business advisors, namely from legal administrative professions such as solicitors, tax consultants, and registered accountants.

*Solicitors* possess a monopoly in legal actions; representation by a solicitor is required in legal proceedings. This can be described as the obligation of a party in a suit to be represented by a university-educated expert who has won

admission to the practice of the law. There is almost no price competition in such advocacy. The Dutch Order of Solicitors publishes an advisory fee schedule consisting of an income component of 60% and a cost component of 40% (of which 20% is personal cost and 20% other cost). However, the differences among fees are not clear. This is because individual solicitors set fees in proportion to (1) the importance of the case (usually expressed in money terms), (2) the degree of difficulty of the case and (3) the time spent on the case.

For registered *accountants* an important domain is reserved through the Registered Accountant Act. The requirement that accountants certify the reliability of the annual accounts of clients as laid down in this law enables the registered accountants to build up a relationship of trust, with the possibility of further advisory practice. However, the most important regulation concerning professional entry is the required training. Because the tariffs of registered accountants are not published and because bills are rarely itemized, fee structures are unknown and price competition is limited.

The technical professions (*town-planning experts, construction engineers* (professional engineers), *interior architects, landscape gardeners* and *consulting engineers*) show many similarities. While in principle entry is free, in practice the vocational training forms an important entry regulation, as it screens out all but the most highly educated groups. Mutual competition exists, but mainly in the shape of quality competition and far less in the form of price competition.

The protection of the position of *real estate agents* is limited to the titles of real estate agent or broker and related words (like brokerage). Restrictions to entry to the occupations of broker or agent in real estate do not exist. Anybody can set up as an intermediary in real estate without any condition other than entering one's name in the Chamber of Commerce. Three conditions must be met to be eligible for swearing-in by a court of law, and consequently to be permitted to bear the title of real estate broker or agent: (1) the candidate has to be well-reputed; (2) no circumstances may stand in the way of a proper and independent pursuit of brokerage activities; and (3) the candidate has to be capable of doing the work. To what extent the title of real estate agent or broker is essential to be successful is hard to say. The brokerage activity has more to do with a fluctuating market than most other professions. This produces significant changes in the volume of the transactions and in the fees charged (the latter because they are related to the amounts of the transactions). Price competition is limited, owing to the application of uniform fees by the brokers, most of whom are members of the Dutch Association of Real Estate Agents.

*The professions in the health care sector* form a distinctive group for want of market competition. There are no close substitutes, so third party competition

is lacking. Moreover, price competition is also absent because of government intervention under authority of the Health Care Fees Act. Also, the relation between price and consumption has been affected by health insurance. In many cases the patient even does not know the price of the medical service he is receiving because the supplier often bills the insurer directly. Entry regulations occur both in the sphere of professional training and through title and profession protection. More or less formal restrictions for establishing a practice are in force concerning general practitioners, medical specialists and pharmaceutical chemists (*e.g.* in the form of arrangements for mutually accommodating client needs for services during non-office hours, which arrangements are indispensable for the actual prosecution of the profession).

### III

#### **Standard Incomes in the Professions**

THUS IT IS CLEAR that market competition is limited in all of the above cases, though to differing degree. Imperfect competition in the market can result in excessive prices and thus in excessive incomes. In the past, the Dutch Government has emphasized that the primary incomes of the professions are made up of three elements: a compensation for the labor involved, a calculated interest on the working capital, and a reward for the entrepreneurial achievement.

As a rule these elements are combined in one stated fee, but the Dutch Government stated in the note of 1975 that they should be separated within the framework of a price policy analogous to the policy pursued in other sectors. This ruling was consistent with the objectives of the fee policy pursued in the mid-70s which concluded that: (a) the income component of the fee was permitted to rise no more than the wages of wage earners, and (b) "price behavior rules" which were applied in the general price policy, were applicable to the cost component.

At the end of 1975 the Government announced that it would apply these rules in a strict way, implying that any existing positive guilder residual (a surplus, after covering practice costs and labor compensation) was not allowed to increase. In 1979, the policy became even more strict in an effort to cut the positive guilder residuals, and in 1980 the Government announced that all positive guilder residuals should be eliminated by the end of 1981. Once this goal is attained, the average income of the professional category it concerns equals the so-called standard income, being a reasonable income from a normative (or political) point of view as determined by the Government. This rule, it should be noted, does not apply to individual incomes, but to averages. Hence, within each profession some inequality of incomes is allowed even if wage and price control is effective, since some earn less and others more than the standard income.

An essential element of such a policy is to fix a standard income for each category of the professions. In 1978 consultations between the Government and the professional bodies about this level led to provisional agreements, to be derived from salary scales of comparable civil servants, chosen by means of job evaluation. The official salary for the private professions is raised by a certain percentage to express the difference in socioeconomic position and in legal status between civil servants and the private professions. This positive differential, mainly concerning differences related to welfare facilities and pension claims, was fixed at 45% in 1978. However, since that time a method has been developed to calculate the component parts of the differential, which procedure will allow for the possibility of different results by professional category. At present, ne-

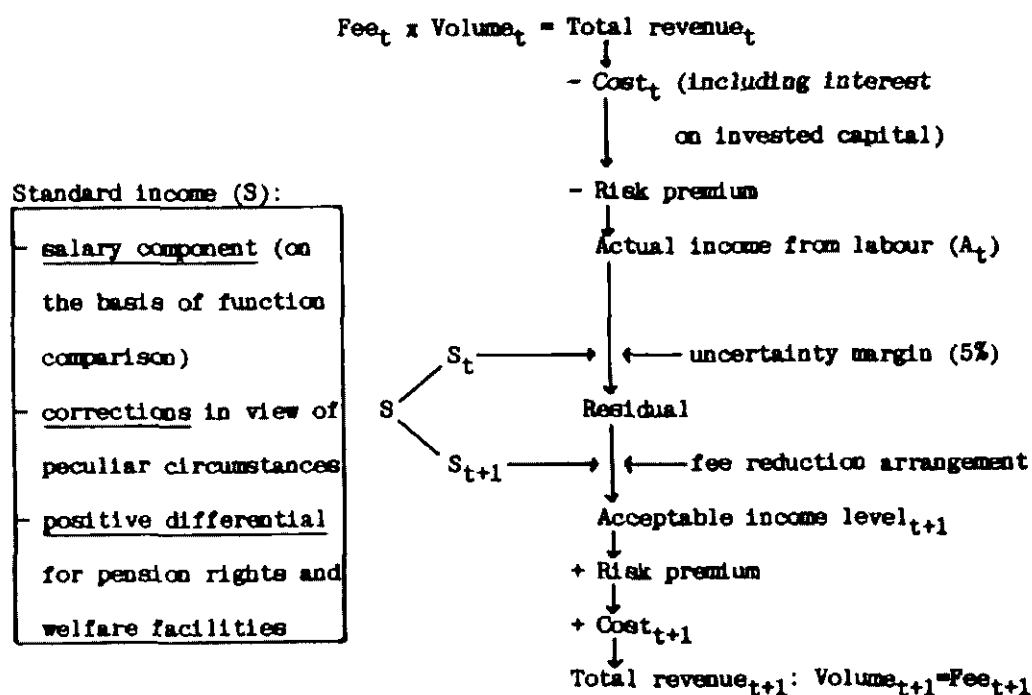


Figure 1. Calculation of Acceptable Income and Fees

gotiations between the government and representatives of professional bodies are attempting to fix the level of permanent standard incomes.

IV

**Implementation of the Standard Income Policy**

THE PRICE/INCOMES POLICY concerning the professions has been implemented initially by promulgating fee decrees for the different professions on the basis of the Price Control Act. Because of legal actions in 1980, it appeared that this act could not be used as an instrument for this policy. The National Medical Specialists Association and four individual medical specialists applied for immediate judgment against the decree as not applying to their professions. The judge ruled that the Government was not allowed to use the Price Control Act for redistribution of incomes.

In response, the Government attempted to solve this problem by inserting explicitly in the Price Control Act the power to achieve acceptable income levels for the professions. This was abandoned, however, on the negative advice of the Council of State. Instead, the Government has chosen (in conformity with the advice of the Council) a temporary statutory regulation: the Act for the Standardization of Incomes of the Professions, acquiring force of law in 1981. This act does not specify the categories of the professions it covers. This responsibility was assigned to the appropriate Cabinet Minister. Since 1982, the formal price control over the fees of the professions in the health care sector has been based on the Health Care Fees Act, but application of the Price Control Act is still possible, particularly if the economic circumstances require the Government to interfere in the fixing of fees at shorter notice than permitted by the Health Care Fees Act.

The way Standard Income is calculated and total revenue (income) breaks down under the (temporary) Act for the Standardization of Incomes of the Professions is shown in the accompanying figure, where  $t$  refers to a certain year followed by year  $t + 1$ . Central to this scheme is the turnover equation: Total revenue = Fee  $\times$  Volume = Cost + Risk premium + Labor income. The total revenue and the cost in year  $t$  follow from an inquiry or are extrapolated by means of the results of inquiries set up in previous years. The actual income from labor in year  $t$  follows from subtracting successively the cost in year  $t$  (including a calculated interest on invested capital) and a risk premium attributable to entrepreneurial activity from the total revenue in year  $t$ . Subsequently the actual income in year  $t$  ( $A_t$ ) is compared with the standard income for that year ( $S_t$ ), taking into account an uncertainty margin, which amounts to 5% at the moment. The latter implies that a residual exists; positive if  $A_t > 1.05 S_t$ , negative if  $A_t < 0.95 S_t$ .

If  $A_t > 1.05 S_t$ , the regulated income in year  $t + 1$  follows from applying a fee reduction arrangement. This arrangement involves either mandated lower fee schedules or a mandated lower rate of increase of fee schedules. The final result, however, might be higher than the standard income because of special circumstances or in connection with residuals which according to the Government are not to be lowered in one year. In these cases, the Government and the law use the term "acceptable income level."

If  $A_t < 0.95 S_t$ , the acceptable income level in year  $t + 1$  is to be fixed at the standard income level for that year. By adding up the expected cost in year  $t + 1$  to the acceptable income level in the same year and taking into account an uncertainty margin again, total revenue in year  $t + 1$  is calculated. Finally, the fee belonging to the acceptable income level in year  $t + 1$  follows from dividing total revenue by the volume.



## V

**The Effectiveness of the Incomes Policy**

IN PRACTICE the implementation of the policy has been restricted to a limited number of professions in the health care sector. The other professions mentioned earlier are not subjected to the incomes policy for at least two main reasons. First, several professions (especially the technical professions and the registered accountants) claim to operate in sufficiently competitive markets. Second, the reluctance of some professional bodies to cooperate, appeared to result in delaying tactics concerning the provision of adequate information about the actual incomes on the one hand and (related to this) the negotiations about acceptable income levels on the other.

In view of the latter it could be expected that the professional bodies would often object to the acceptable income levels as proposed by the Government. In that case the Minister consults a (provisional) advisory committee being

Table 1.  
Acceptable income levels for professional categories, 1982 - 1984  
and the comparable civil servants' salaries, 1984

professional category	acceptable income level (Dutch guilders)			comparable civil servants' salary
	1982	1983	1984	1984
dental specialists				
- for mouth diseases and jaw surgery <sup>a)</sup>	220.900	202.700	192.700	126.200
- in the dentomaxillar orthopaedy <sup>a)</sup>	219.200	196.000	186.000	126.200
pharmaceutical chemists	147.300	147.200	147.200	106.100
general practitioners	147.300	143.600	143.600	103.300
dentists	135.500	135.400	135.000	97.600
speech therapists	76.800	76.400	75.400	55.200
physiotherapists	67.500	67.400	67.400	48.100
obstetricians	64.900	64.800	63.900	46.100

a) The differences in acceptable income levels indicate a difference in positive residuals

composed of three members. For example, in 1983 the organizations of general practitioners, dentists, dental surgeon specialists, physiotherapists, pharmaceutical chemists, obstetricians and speech therapists did object to the Government's acceptable income levels proposals. Although the Government is urged to consult the provisional Advisory Committee for the Incomes of the Professions in such a situation, the advice given is not legally binding.

A serious problem is that the comparison of the actual income with the standard income is hindered by a lack of current and reliable information on the former. Earlier I drew attention to the length of the elapsed period between the moment of decision to conduct an inquiry into the incomes of the professions and the moment of publication. As a result of this long delay, the findings of the inquiry were no longer relevant to the policy being pursued. As of the beginning of 1984, this situation remained unchanged. According to a letter the Government

sent to the Parliament, the Government is again consulting with a number of professional bodies so as to make new estimates.

As an illustration of the problem which the Government confronts, the regulations were unable to fix acceptable income levels for medical specialists in 1983 and 1984 because of the great uncertainty concerning their actual incomes. Even though a draft arrangement exists requiring the medical professions to furnish the relevant income data, the Government concedes that the data collection will continue to be problematic, even if legally required.

The lack of current and reliable information on the actual incomes of the professions is a serious problem in evaluating the effectiveness of the price/incomes policy for the professions. Table 1 shows for several professional categories both the acceptable income levels as fixed in the period 1982–1984 and the comparable civil servant's salaries in 1984. The majority of the acceptable income levels shown in this table appears to be fixed consecutively on a lower level.<sup>12</sup> But whether the actual incomes in 1984 have declined in comparison to the previous years is not known.

However, it can be observed that judicial problems obviously made it impossible to realize the purpose sought in 1980 that all positive residuals should have disappeared by the end of 1981. The Government itself has admitted that there were still positive residuals in 1984. In this sense the policy has not been effective. The response of the professional bodies to the policy in terms of their reluctance to provide the necessary information can also be interpreted as an indication of the ineffectiveness of the policy. Thus, the experience gained by applying the Dutch incomes policy to the professions can be seen as a case study of the power of private interests to subvert the general public interest.

## VI

### Concluding Remarks

IN THE NETHERLANDS, it is an accepted principle that private professional income should be comparable with that of officials and civil servants with comparable training and responsibilities. Within the framework of the price/incomes policy, the acceptable income levels for the professions are fixed for each category and are derived from official salary scales. As Table 1 shows, acceptable income levels fixed for 1983 and 1984 tend to be lower than in 1982. However, while the price/incomes policy affects the *acceptable* income levels of the professions, there are serious doubts whether the *actual* 1983 and 1984 incomes of the professions have declined at the same rate as the acceptable income levels or, indeed, have declined at all. However, the effectiveness of the price/incomes policy for the professions cannot be determined with certainty because of a lack of current and reliable data on the actual incomes of the professions.

**Notes**

1. See De Jong (1972), p. 156.
2. See Brittan and Lilley (1977), p. 121.
3. This is illustrated in Chater, Dean and Elliott (1981).
4. As pointed out by Blackaby (1972), p. 217.
5. Compare De Wolff (1983); Flanagan, Soskice and Ulman (1983); "Industrial Democracy in Europe" (IDE) International Research Group (1981), Kennedy (1980), Tinbergen (1975) and Windmuller (1969).
6. In general terms, professions are characterized by their requirement of intellectual or specialized skills provided to patients or clients on a personal, direct basis, and hence their practitioners must have undergone extensive preparatory training. The Minister of Social Affairs formally specifies which particular professions are subjected to the incomes policy. Other Ministers can be involved with respect to certain aspects of the implementation of the policy, especially the Minister of Health Care as far as the professions in the health care sector are concerned. As pointed out in Section V, practice thus far has shown that in fact only *the professions in the health care sector* have been subjected to the incomes policy.
7. For a thorough discussion of this topic see Olson (1982).
8. The total remuneration is thought to be composed of a return for the achieved labor, a calculated interest on the working capital and a reward for the entrepreneurial achievement. The term labor element refers to the first category.
9. This working group (established in 1972) is made up of representatives of the organizations of the professions, the Ministry of Economic Affairs, the Ministry of Social Affairs and the Central Bureau of Statistics. The task of this working group was to examine the possibilities of an inquiry into the labor element of professional earnings, which should make it possible to compare these earnings with those of comparable wage earners in the Government and the private sector.
10. Although the Government does not clarify the concept of normal market structure, it can be assumed that a competitive market is meant.
11. It should be noted that these fees are set by the professional body itself.
12. Because these are nominal amounts, the acceptable income levels have declined more in real terms

**References**

- Blackaby, F. (1972), "Incomes Policies: A Background Paper," In *An Incomes Policy for Britain*, ed. by F. Blackaby (London: Heinemann Educational Books), pp. 217-36.
- Brittan, S. and P. Lilley (1977), *The Delusion of Incomes Policy* (London: Temple Smith).
- Chater, R. E. J., A. Dean, and F. Elliott, eds. (1981), *Incomes Policy* (Oxford: Clarendon Press).
- De Jong, J. R. (1972), "National Wage and Job Evaluation in the Netherlands," In *An Incomes Policy for Britain*, edited by F. Blackaby (London: Heinemann), pp. 145-60.
- De Wolff, P. (1983), "Income Policy Developments in the Netherlands," *Industrial Relations*, Vol. 22, No. 2 (Spring 1983), pp. 203-23.
- Flanagan, R. J., D. W. Soskice, and L. Ulman (1983), *Unionism, Economic Stabilization and Incomes Policies: European Experience*, (Washington: The Brookings Institution).
- Industrial Democracy in Europe (IDE) International Research Group (1981), *European Industrial Relations* (Oxford: Clarendon Press).
- Kennedy, T. (1980), *European Labor Relations* (Lexington: D. C. Heath and Company).
- Olson, M. (1982), *The Rise and Decline of Nations* (New Haven and London: Yale Univ. Press).
- Tinbergen, J. (1975), "Education, Inequality and Life Chances: A Report on the Netherlands," In *Education, inequality and life chances*, Vol. 2 (Paris: OECD), pp. 404-26.
- Windmuller, J. P. (1969), *Labor Relations in the Netherlands* (Ithaca, N.Y.: Cornell Univ. Press).

Copyright of American Journal of Economics & Sociology is the property of Blackwell Publishing Limited. The copyright in an individual article may be maintained by the author in certain cases. Content may not be copied or emailed to multiple sites or posted to a listserv without the copyright holder's express written permission. However, users may print, download, or email articles for individual use.