International Labour Organization

General Process for Sustainable Social Protection Policy Reform

Fiscal Space/Financing Options

Improving Synergies between Social Protection and Public Finance Management

Helmut Schwarzer (Public Finance Economist – SOCPRO/ILO) E-mail: Schwarzer@ilo.org

Workers in Turkey. © ILO.

Quiz – Are you knowledgeable about global taxation?

1. **Which country has the highest total tax revenue as a % of GDP (source: OECD 2018)?**

    A. Cuba, B. France, C. Nauru, D. Sweden

2. **How much is the revenue from social security contributions collected by France (% of GDP, source: OECD 2018)?**

    A. 9,0%, B. 14,5%, C. 15,4%, D. 16,0%

3. **Which country has the highest participation of social security contributions as a percentage of total tax revenue (source: OECD 2018)?**

    A. Belgium, B. Costa Rica, C. Germany, D. Uruguay

AFORE Movil, Mexico © Omar Flores

Structure proposed

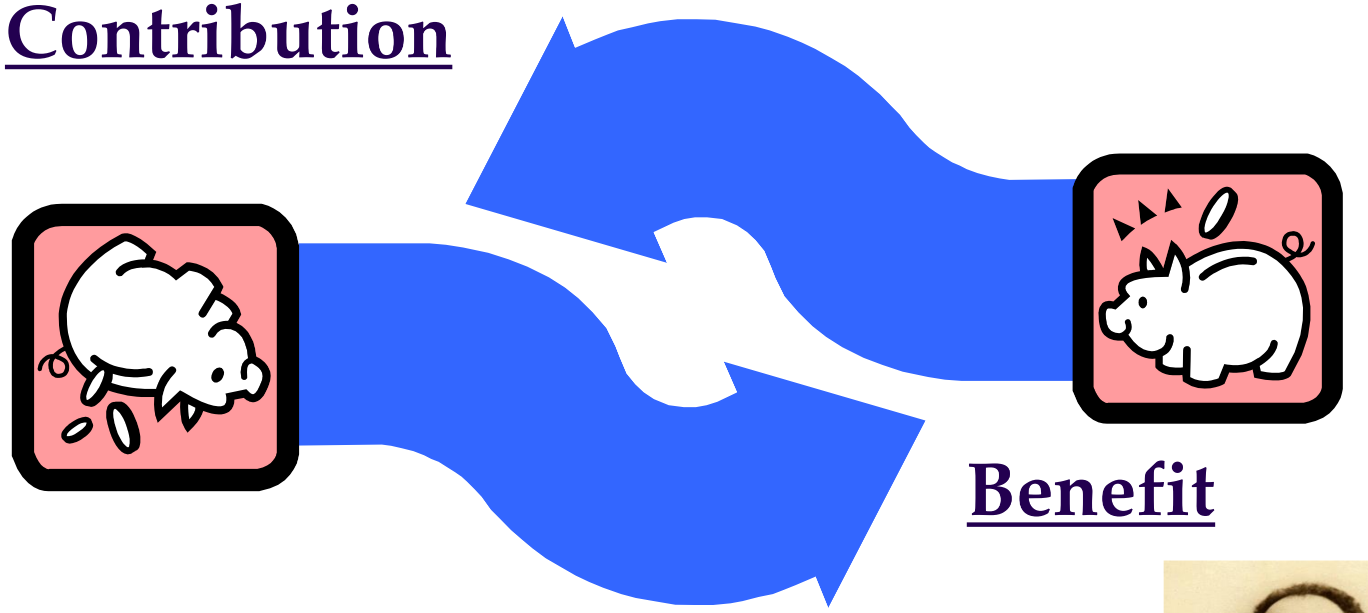
- Concepts on Financing
- The Policy Dialogue
- Tools to Support the Dialogue
- Fiscal Space and Possible Sources
- Country Case of Fiscal Space

Workers in Jordan. © ILO.

International Labour Organization

Social Security: A savings relation seen from the individual perspective?

Contribution



Benefit

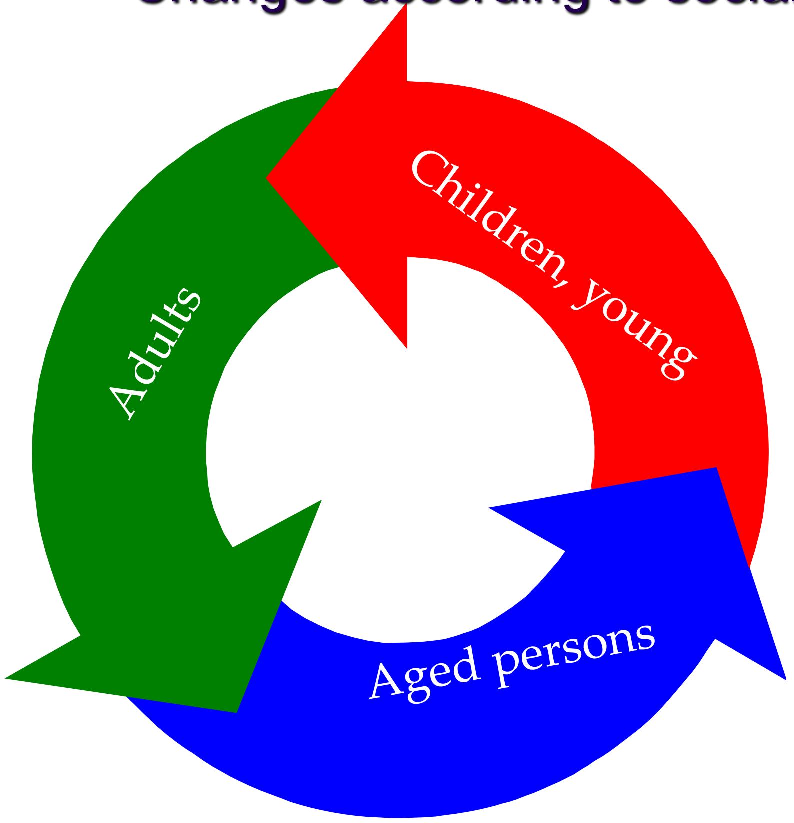
Eugen v. Böhm-Bawerk (1889): utilitarianism, “myopia” and preference for present over future consumption – the concept afterwards was used to sustain the mandatory affiliation to social security.

Social Security: A time machine that transfers money?

International Labour Organization

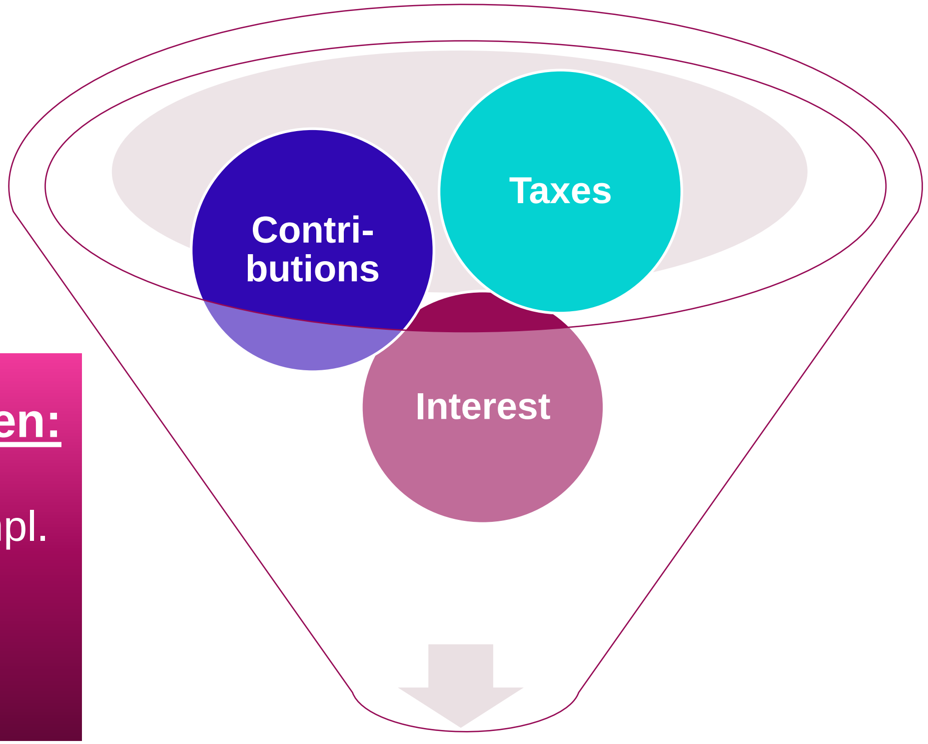
A complex social contract:

- Multiple generations;
- Intra- and inter- generational transfers;
- Complex financing;
- Changes according to social preferences.



<u>Solidarity between:</u>
Adults ↔ Aged
Employed ↔ Unempl.
Healthy ↔ Sick
Sane ↔ Injured
Etc.

F. Mackenroth (1952): "Financing will always come from the current output"



Financing of Social Protection

"Even if important for the balance and operation, the option for a financing method doesn't change the fact that all fiinancing has to come from the current output."

“The three worlds of Welfare Capitalism” (Gøsta Esping-Andersen, 1990)

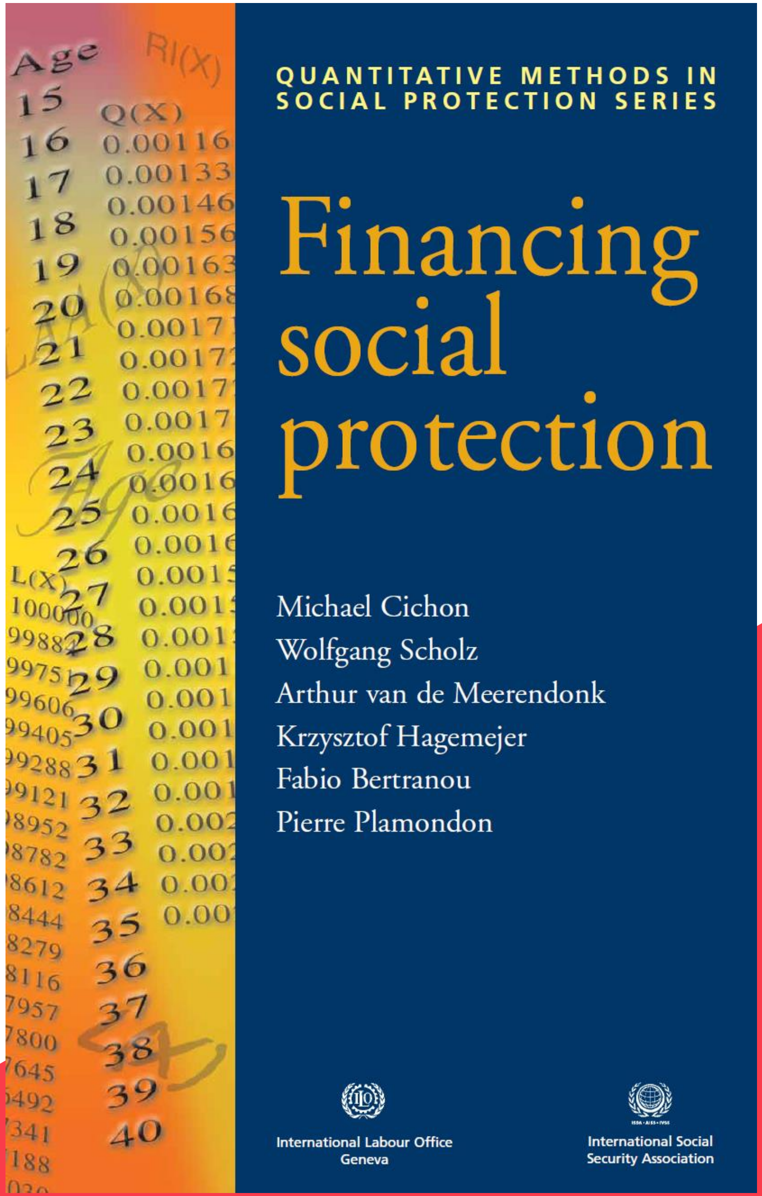
Social Insurance	Universal Coverage	Fight against Poverty
Right comes from contribution	Right comes from being part, belonging	Right comes from need
Financed from contribution revenue	Financed via contributions and taxes	Financed via taxes
Bismarkian Welfare State	Social-Democratic Universalism	Residual / Assistential Welfare State

International Labour Organization

Financing Social Protection

Cichon, M., et al. (2004). Financing social protection. Quantitative Methods in Social Protection Series.

https://www.social-protection.org/gimi/ShowRessource.action?id=8030



Why finance social protection?

"Effective financing systems ensure that benefit promises are reasonable and can be kept." (Cichon, M. et. al., Financing Social Protection, p.1)

"Aiming for equity means that the burden of financing social protection is shared fairly among population groups and generations. Aiming for financial, fiscal and economic efficiency means making sure that no societal resources are wasted – and thus no welfare losses incurred – when financing systems are designed or operated." (Ibid.)

Worker, Tuxtla Gutiérrez, Mexico © OIT

5 basic questions that define a financing system (Cichon et. al., cap. 5 pp219 ff)

"By selecting specific financing systems", societies determine "the way in which the income needed to finance different social benefit schemes will be generated." (p. 220)

Question 1	Question 2	Question 3	Question 4	Question 5
Who pays…	… from what inome…	… what amounts...	… in what moment of time…	… for whom?
Groups covered	Source of financing	Rules of financing	Actuarial/ fin. balance rule	Group covered

Combination of sources and methods in financing social security regimes

- Taxes – General and specific ones (“earmarked”)
- Contributions – employer / worker
- Interest resulting from reserve investments
- Others (usually residual)

Pay as you go

- Revenue of present year finances benefits of present year
- May have contingency / fluctu-ation / emergency reserves

Partial capitalization

- Scaled premium;
- PYGO with coverage of liabilities created in the year

Full capitalization

- All liabilities of the regime are covered by a reserve
- Collective or individual

Financing mechanisms: contributory and non contributory regimes

Contributory
(financed mainly by contributions)

- Social Insurance;
- Occupational Regimes;
- Provident Funds;
- Mutuality, community-based insurance, microinsurance.

Non contributory
(financed mainly by taxes)

- Universal regimes;
- Categoric regimes;
- Assistential / targeted regimes including CTs, conditional or not;
- Employment guarantee regimes.

Young women, Tuxtla Gutiérrez, Mexico © OIT

The process of policy development

International Labour Organization

1 Inventory of existing social protection schemes and data

2 Identifying and estimating coverage gaps

3 Costing analysis and projections of financing needs

4 Conducting fiscal space analysis

5 Poverty impact assessment

6 Policy recommendations

You are supporting a Public Policy Process:

"Agenda Setting, Discourse Creation, Coalition Forging, Getting Agreement, Learning Processes, Reframing Problems, Networks Feasibility/Interests/Power, Economic Constraints, Appropriation, etc."

The process of policy development

1. Inventory of existing social protection schemes and data
2. Identifying and estimating coverage gaps
3. Costing analysis and projections of financing needs
4. Conducting fiscal space analysis
5. Poverty impact assessment
6. Policy recommendations

Social dialogue

Capacity building

Policy Actors: Tripartite Constituents, Interested Parties, Government Agencies

Building a favourable environment - "Arena", Establish Rules of the Dialogue that allow for reaching convergences and results.

Woman, Tuxtla Gutiérrez, Mexico © ILO.

The process of policy development

Process

1. Inventory of existing social protection schemes and data
2. Identifying and estimating coverage gaps
3. Costing analysis and projections of financing needs
4. Conducting fiscal space analysis
5. Poverty impact assessment
6. Policy recommendations

How to

- Social dialogue
- Capacity building

Tools

- **ABND/SPOTT methodologies**
- **SSI (Social Security Inquiry)**
- **RAP costing tool**
- **ILO/HEALTH**
- **ILO/PENSIONS**
- **Handbook on fiscal space**
- **Poverty impact assessment tool**

Tools to be used to promote and strengthen national appropriation, "ownership"

The process of policy development

Usually, a policy process is less linear than shown in the textbooks. Reinforcing "previous" steps is no loss of time.

Process

1. Inventory of existing social protection schemes and data
2. Identifying and estimating coverage gaps
3. Costing analysis and projections of financing needs
4. Conducting fiscal space analysis
5. Poverty impact assessment
6. Policy recommendations

How to

Social dialogue

Capacity building

Tools

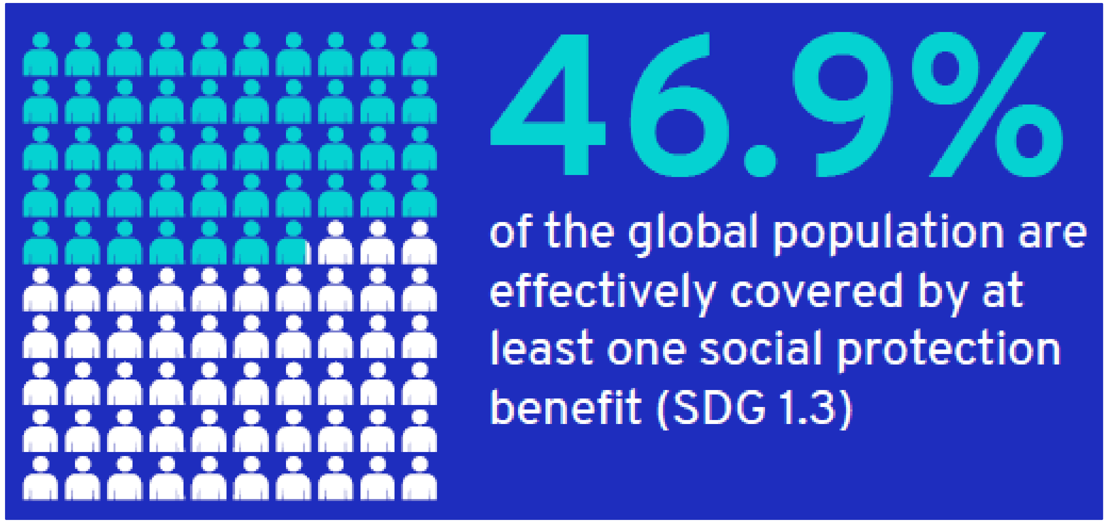
- **ABND/SPOTT**
- **SSI (Social Security Inquiry)**
- **RAP costing tool**
- **ILO/HEALTH**
- **ILO/PENSIONS**
- **Handbook on fiscal space**
- **Poverty impact assessment tool**

Expected results

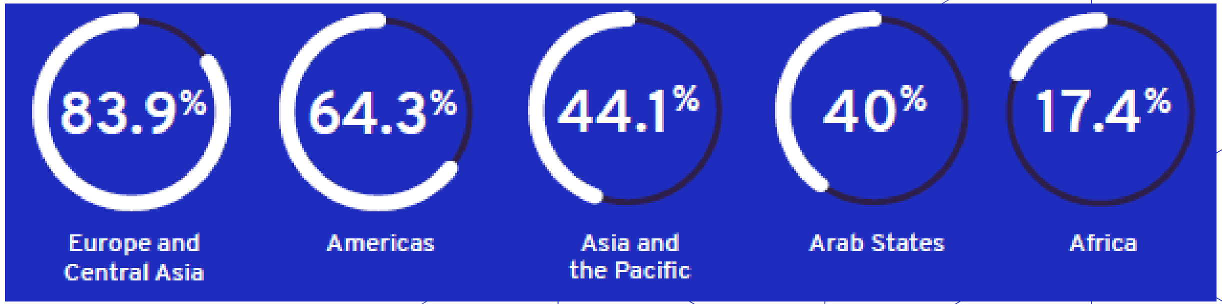
- **Create confidence and support a national consensus through social dialogue.**
- **Shared understanding of the national SP system configuration at the country level**
- **Policy options and costs of extending social protection coverage**
- **Policy and Financing gaps identification**
- **Quantification and feasibility analysis of different options to create fiscal space**
- **Measure impact on poverty ~~linked to~~ of different SP policies**
- **Strategies for extending social protection (informal sector, women, rural, specific populations)**

World Social Protection Report 2020-22

Despite the unprecedented worldwide expansion of social protection during the COVID-19 crisis, more than 4 billion people around the world remain entirely unprotected.



Indicator to monitor progress on SDG target 1.3 (Universal Social Protection)



Tools to help during each of the steps

Social Security Inquiry- SDG indicator 1.3.1

Dimension 1: Spending and financing

- Who is paying (financing sources)?
- What is the cost (how much for the benefits, how much for the administration)?

Dimension 2a: Social protection coverage

- Who is covered: How many (poor- non poor, employees/ own-account workers, contributing family workers; workers in formal/ informal employment, men/women)?
- What are the benefits provided (risks covered)?

Dimension 2b: Social protection benefit level

- What is the amount of benefit?

ILO | Social Protection platform | **World Social Protection Data Dashboard** | Language: English | Login

International Labour Organization | World Social Protection Data Dashboards

Home | SDG 1.3.1 | Data Dashboards | Data compilation | Resources | Glossary | About us | Contact us

tools

SOCIAL SECURITY INQUIRY

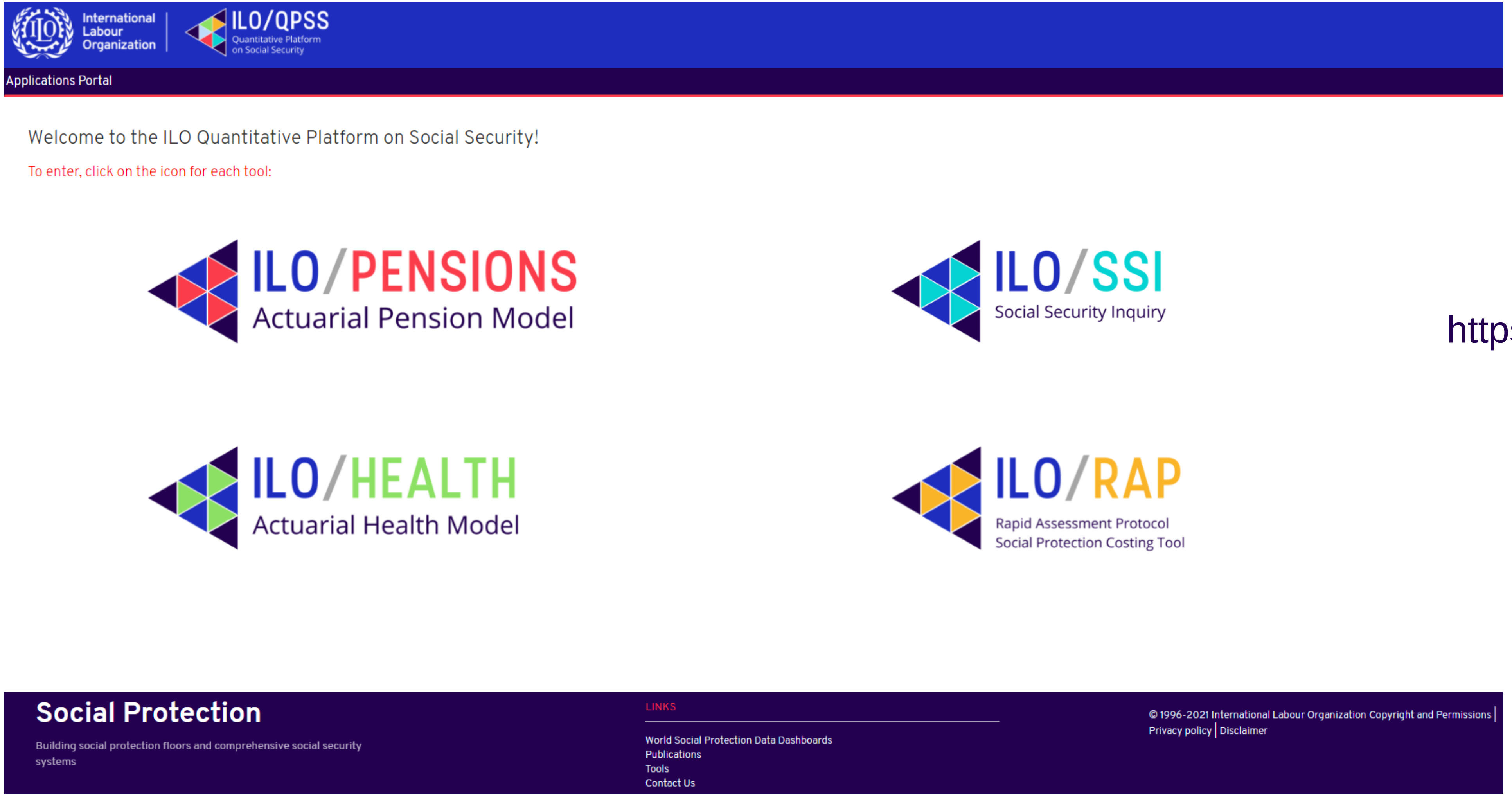
Social Security Inquiry (SSI) questionnaire has become the main comprehensive tool used to compile data on social protection coverage for children, unemployed persons, older persons, persons with disabilities, women with newborns, work-injury victims, and the poor and the vulnerable. In addition, indicators on adequacy of social protection benefits and the revenue and expenditure of the social protection schemes are being produced based on the data provided in the questionnaire. Social Protection Department has been disseminating comparable statistics on global social protection programs periodically via thematic studies as well as the ILO Flagship World Social Protection Report, which is published triennially and includes information on legal and effective coverage of social protection systems, description of contributory and non-contributory programmes, indicators of adequacy of benefits, social protection expenditure and others for more than 190 countries. The latest report was published in 2017 - World Social Protection Report 2017-2019: Universal social protection to achieve the Sustainable Development Goals.

Learn more about the SSI

- Social Security Inquiry Questionnaire - Online version (for registered users)
- Social Security Inquiry Questionnaire - Excel version (EN), (ES), (FR), (PT)
- Getting Started Guide (EN), (ES), (FR), (PT)
- Technical Guide (EN)
- Social Security Inquiry Questionnaire (including a module on migrant workers - EN) and Getting Started Guide

https://www.social-protection.org/gimi/gess/WSPDB.action?id=41

QPSS – Quantitative Platform on Social Security

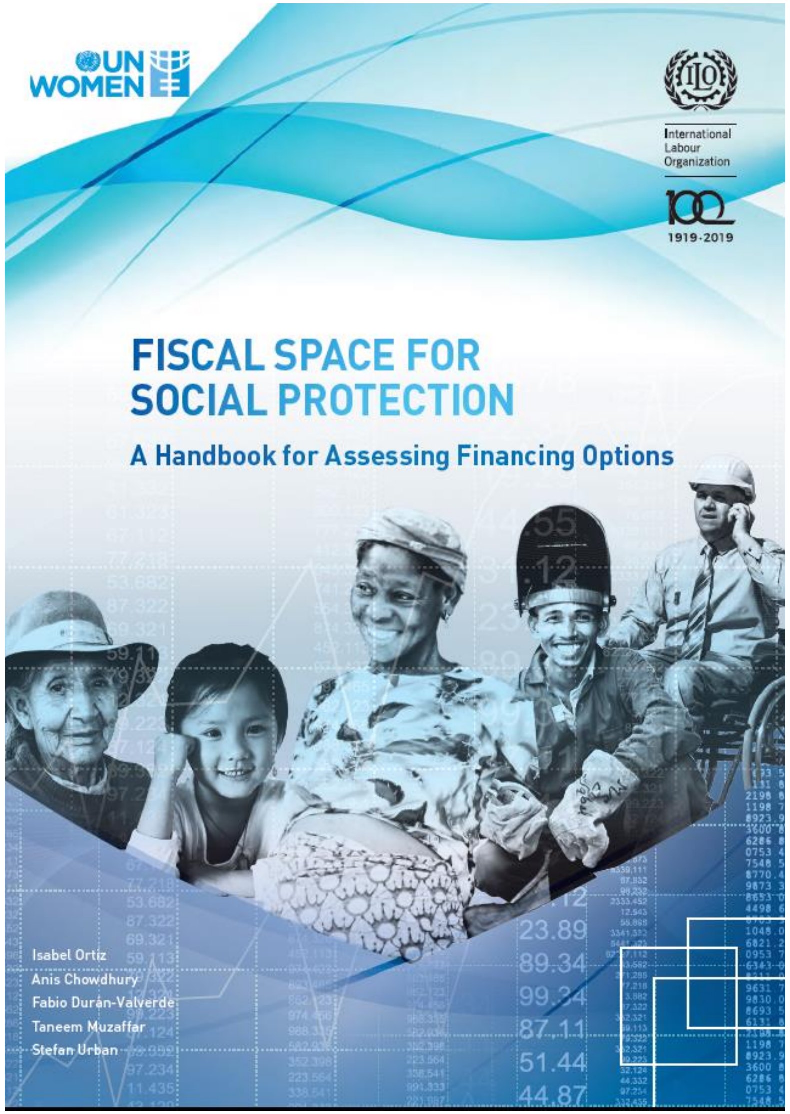


https://qpss.ilo.org/

Fiscal Space for Social Protection

- Fiscal space is defined as the resources available as a result of the active exploration and utilization of all possible revenue sources by a government. (ILO, UNICEF, UNWomen, 2020)

- Fiscal space exists if a government can raise spending or lower taxes without endangering market access and putting debt sustainability at risk. (IMF, 2016)



Key Messages – Fiscal Space for Social Protection

International Labour Organization

States must use all possible resources to realize human rights

Need to create fiscal space has never been greater.

There are multiple options to expand fiscal space for social protection.

Competing and reducing space for other social policies is not one of them.

Uniqueness of each country requires specific analysis.

It is key to inform and submit the options to a national dialogue.

Worker, Tuxtla Gutiérrez, Mexico © ILO

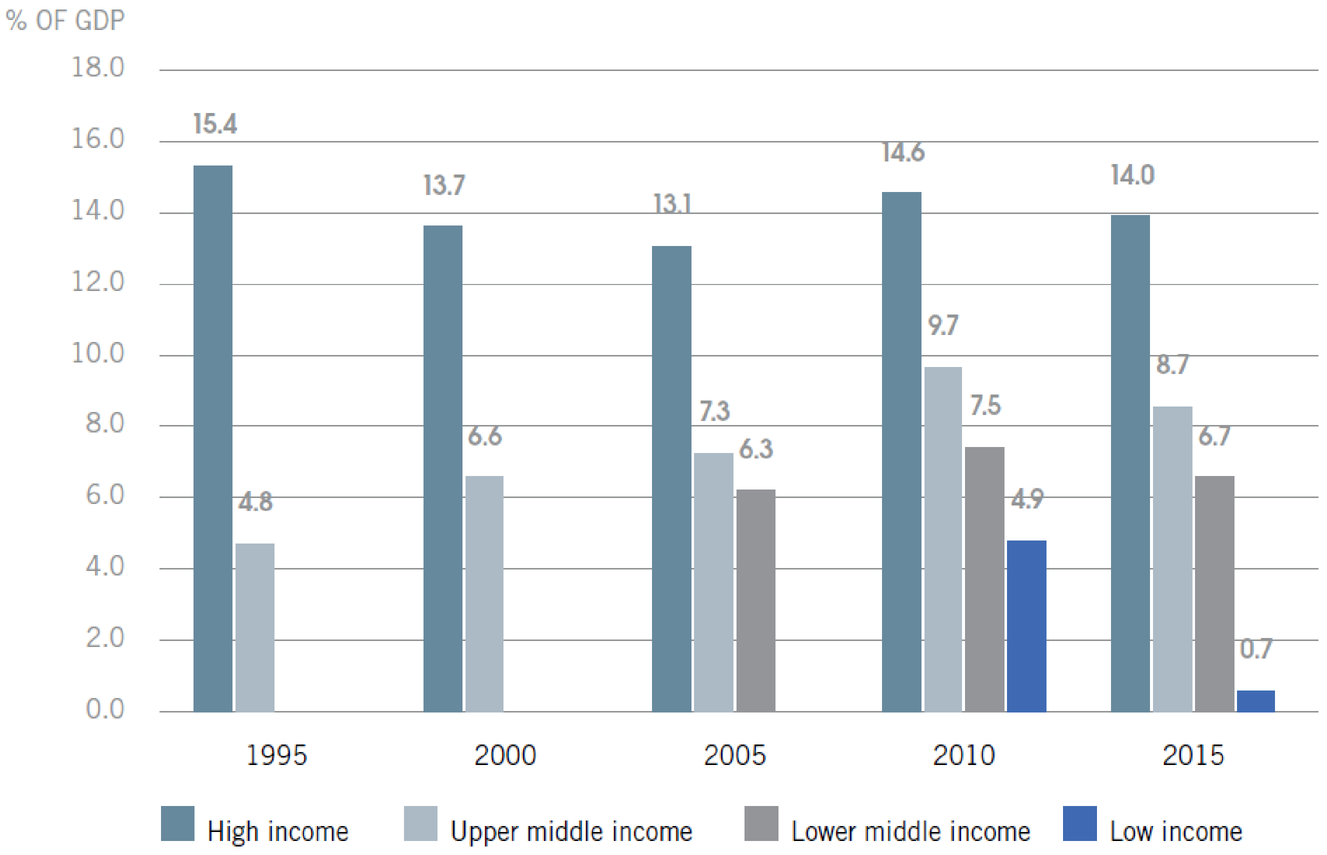
Figure: Trends in public social protection expenditure (income groups; per cent of GDP) – p.25

Expenditure indicators

The main indicators used to analyse financing at the broadest level are government revenue and expenditure as a percentage of GDP.

A subset of government expenditure is various public social expenditure such as on education, health, and social security/protection, etc., as percentages of GDP.

Revenue-GDP and expenditure-GDP ratios adjust for the income level, and are suitable for cross country comparison.



Source: IMF, Government Finance Statistics (various issues)

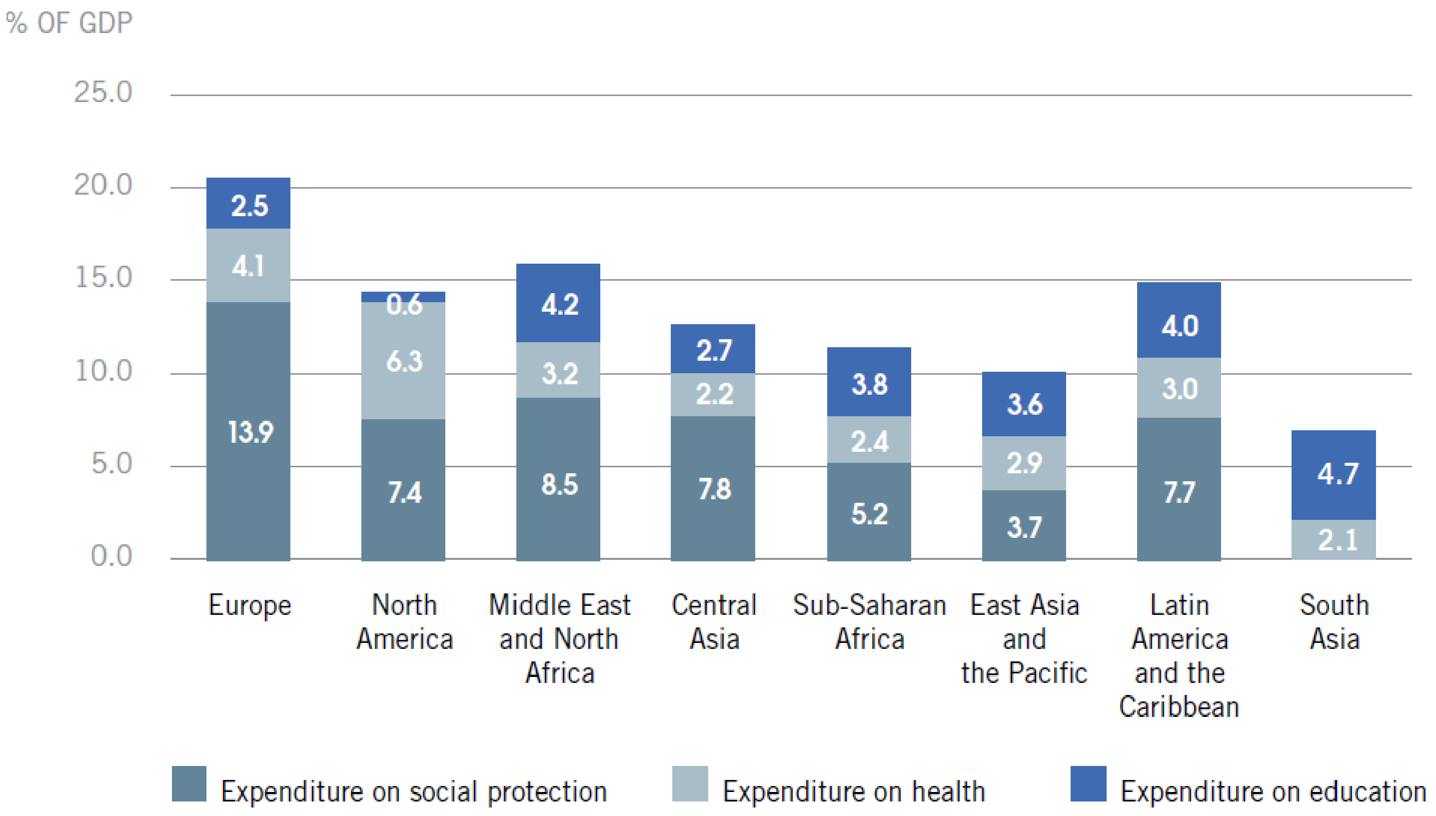
Expenditure trends

It is essential not to confuse social protection expenditure with other social sector expenditures such as education.

Expenditures in one social sector should never displace expenditures in another social sector.

Public investments in all social sectors are needed as part of national development strategies and governments should look to expand fiscal space to have adequate investments in all sectors.

Figure: Composition of public social spending in 2014, by world regions – p.24



Note: Based on IMF regional classification.
Source: IMF Government Finance Statistics.

International Labour Organization

Key messages - Social protection financing: Indicators and trends

- Analysing public finance – revenues and expenditures – is often hampered due to problems associated with data availability, quality, frequency and disaggregation, besides the lack of uniformity in methodologies used by countries and international organizations.

- Social protection spending does not necessarily depend on a country income level or overall government spending; social protection systems require a politically sustainable social contract.

- Social protection is an important investment, it increases productivity and human capital, fosters domestic demand and promotes political stability - the most productive world economies committed to social spending in the early stages of their development.

- Some argue that social protection policies are not affordable in developing countries. But ultimately, affordability depends on a society's willingness to finance social protection policies.

Eight options to extend fiscal space (ILO, UNICEF, UNWomen, 2020)

Eight financing options that countries should analyse and discuss in national dialogues:

1. Expansion of coverage of social security and contributory revenue;
2. Increase of tax revenue;
3. Elimination illicit financial flows;
4. Increase efficiency of public expenditure and reallocation to social protection prioritary areas;
5. Use of exceding fiscal and foreign exchange reserves;
6. Debt or restructuration of debt;
7. Adoption of a more flexible macroeconomic frame;
8. Increase of ODA and other forms of foreign aid.

https://www.social-protection.org/gimi/gess/ShowRessource.action?id=55694

Student, Tuxtla Gutiérrez, Mexico © OIT

Estimates to close social protection gaps

International Labour Organization

- Considering the impact of the COVID-19 pandemics, ILO estimated the fiscal effort needed to close the gap of 4 billion people without social protection.
- A Social Protection Floor composed by essential health (following WHO definitions) and cash transfers for children, disabled, aged and maternity was estimated.
- Globally, the effort required for developing countries is of US$ 1.2 trillions, equivalent to 3.8% of GDP.
- Social contributions represent today 57.2% of the financing of social protection in the world.
- ILO estimates that the revenue of social contributions can increase by 1.2% of the GDP, from 5.1% to 6.3%, helping to close the gap.

SP Expenditure, 2020

ILO (2020). Financing gaps in social protection: Global estimates and strategies for developing countries in light of the COVID-19 crisis and beyond.

Worker during COVID-19, Harare © ILO.

Conclusions

1. Coverage and financing gaps affect virtually all regions of the world, especially developing countries.
2. Social security contributions and general taxation are fundamental sources of fiscal space.
3. Middle-income countries have capacity to increase domestic resources to close the gap. Transition to formalization is important part of the strategy. South-south exchanges.
4. In low-income countries, the financing gap represents approximately 45% of their tax revenue. Therefore, massive international solidarity is essential.

Worker, Tuxtla Gutiérrez, Mexico © OIT

International Labour Organization

Country experience: Albania

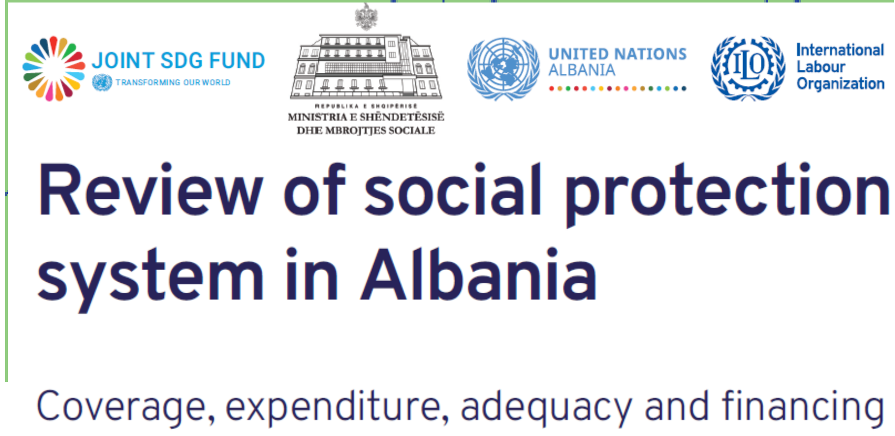
Financing Social Sectors for Vulnerable Groups

27 September 2021

Kenichi Hirose
Senior Social Protection Specialist
ILO Decent Work Technical Support Team for Central and Eastern Europe
Email: hirose@ilo.org

International Labour Organization

Assessment of fiscal space for social protection in Albania



Available at:
https://www.ilo.org/budapest/what-we-do/publications/lang--en/index.htm

Structure of the Study on Fiscal Space (Ex. Albania)

International Labour Organization

Contents

Albania, Streetvendor. © Twitter Janet King.

Albania: Two UN Joint Programmes funded by the Joint SDG Fund

- Catalyzing municipal social protection
- Strategic policy options for SDG financing

Map Albania © Factmonster

International Labour Organization

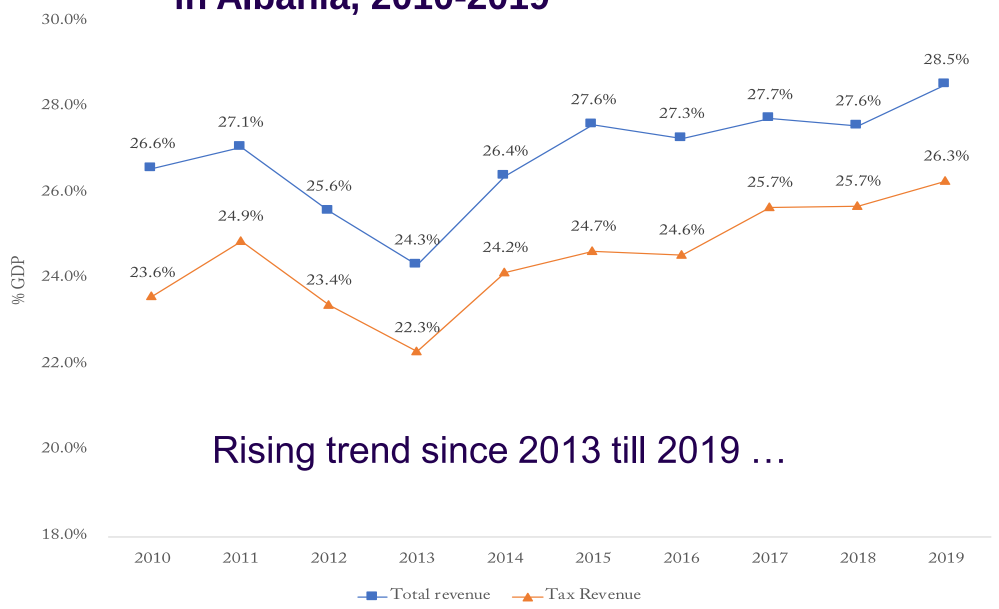
ILO contributions

- Review of the social protection system in Albania
- Assessment of fiscal space for social protection
  - Analyzes gaps in the financing of social protection
  - Develops options to create fiscal space for building a comprehensive system including national social protection floors
- Assessment, design and costing of social protection programmes
  - Childcare and child allowance
  - Long-term care benefits and services
  - Assessment of the targeting of economic assistance
- Feasibility study of innovative financing mechanisms.
- Financing options for a shock responsive social protection including the response of COVID-19
- Policy dialogue amongst national stakeholders

Fiscal space options for Albania (1)

1. The twin shocks to the economy have significant implications for public finance – deteriorating revenue collection and rising fiscal deficits.
2. The report analyses fiscal space options based on historical data before the pandemic.
3. Ministries of Finance/Planning should explore all possible fiscal scenarios and options, associated social impacts including gender issues, risks and trade-offs.
4. The set of alternative policy options for inclusive development should be discussed amongst all stakeholders in a **national social dialogue**.

Trends in total revenue and tax revenue in Albania, 2010-2019

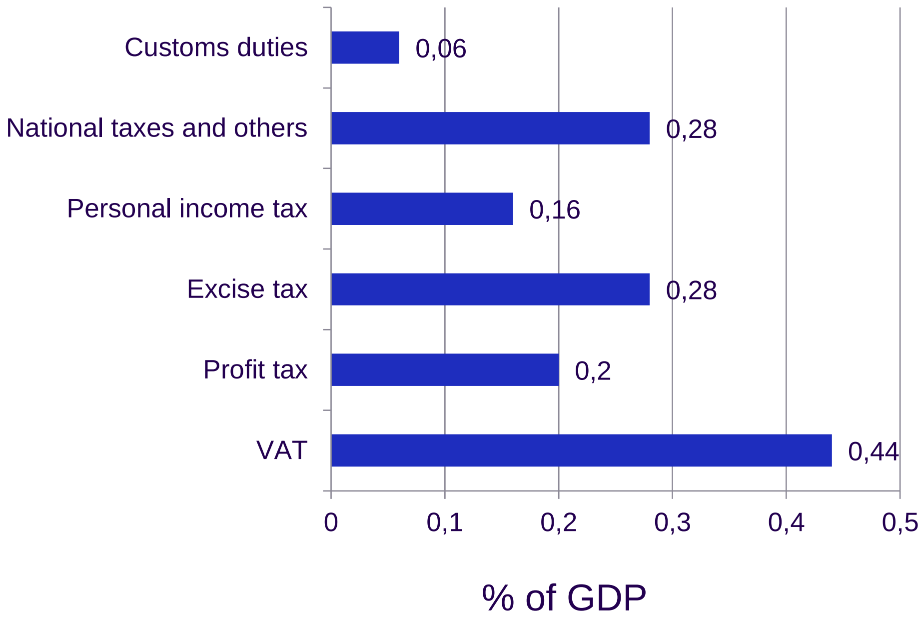


… but fiscal revenue in 2020 under pressure due to economic contraction and measures to reduce or defer taxes. Tax revenue during Jan-Sept 2020 down by 10.6 per cent (y-o-y) (Source: IMF).

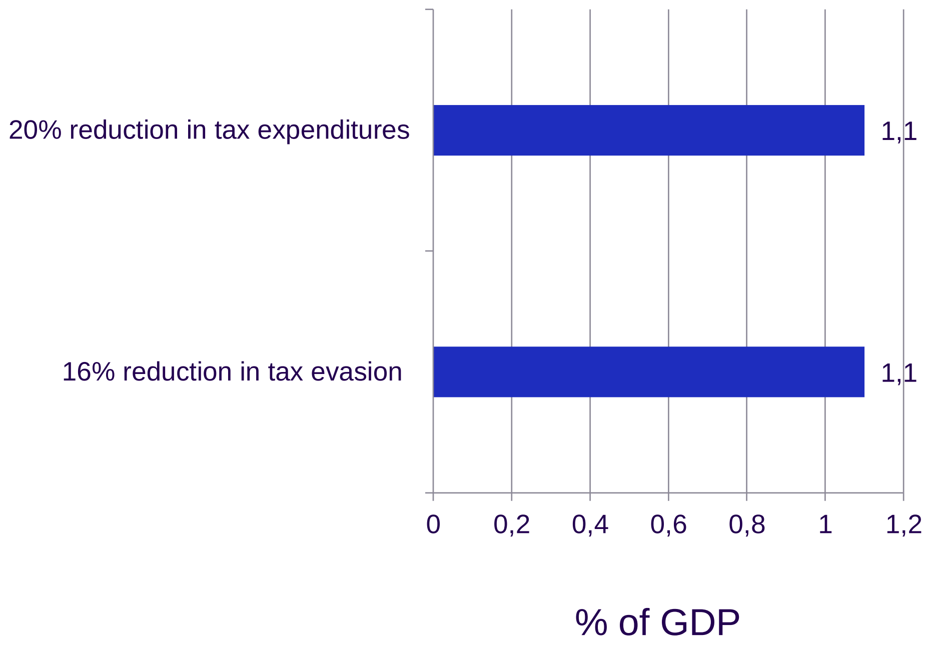
Fiscal space options for Albania (2)

Taxation

1. Estimated additional resources from increasing tax rates by 1 percentage point



2. Estimated additional resources from reducing tax expenditure and evasion

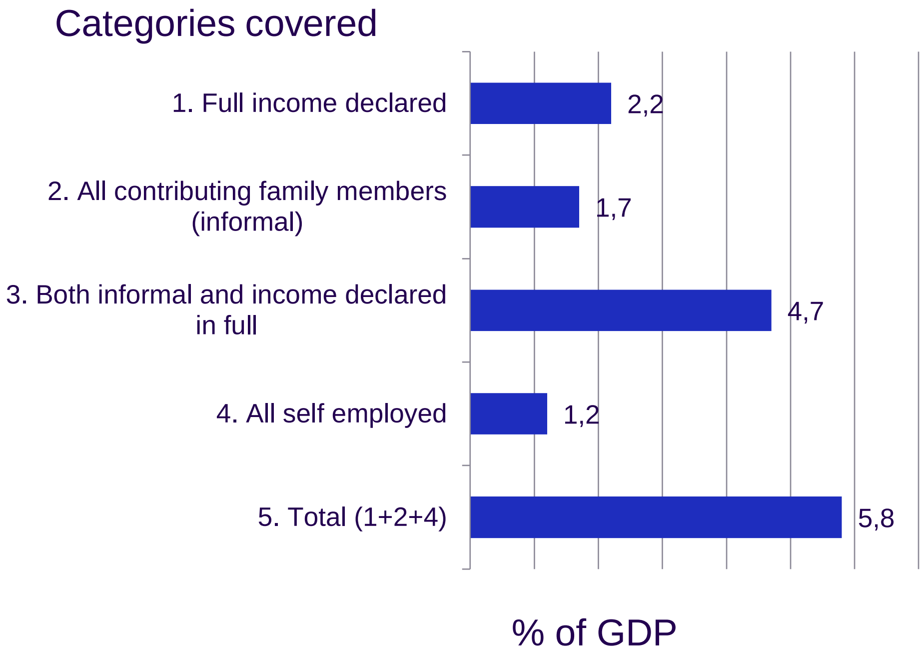


International Labour Organization

Fiscal space options for Albania (3)

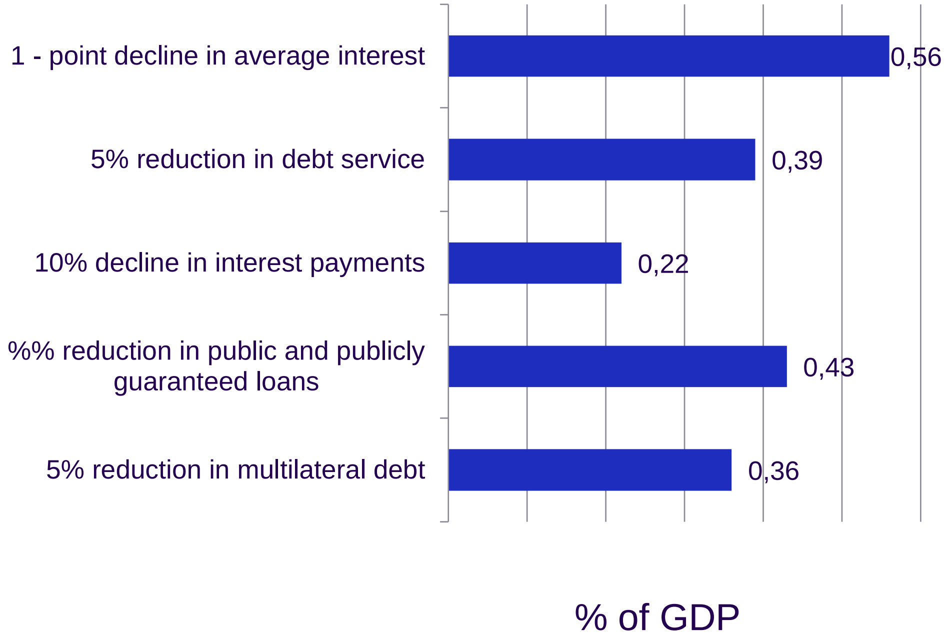
Social security contributions

Estimated additional resources from increasing social insurance coverage

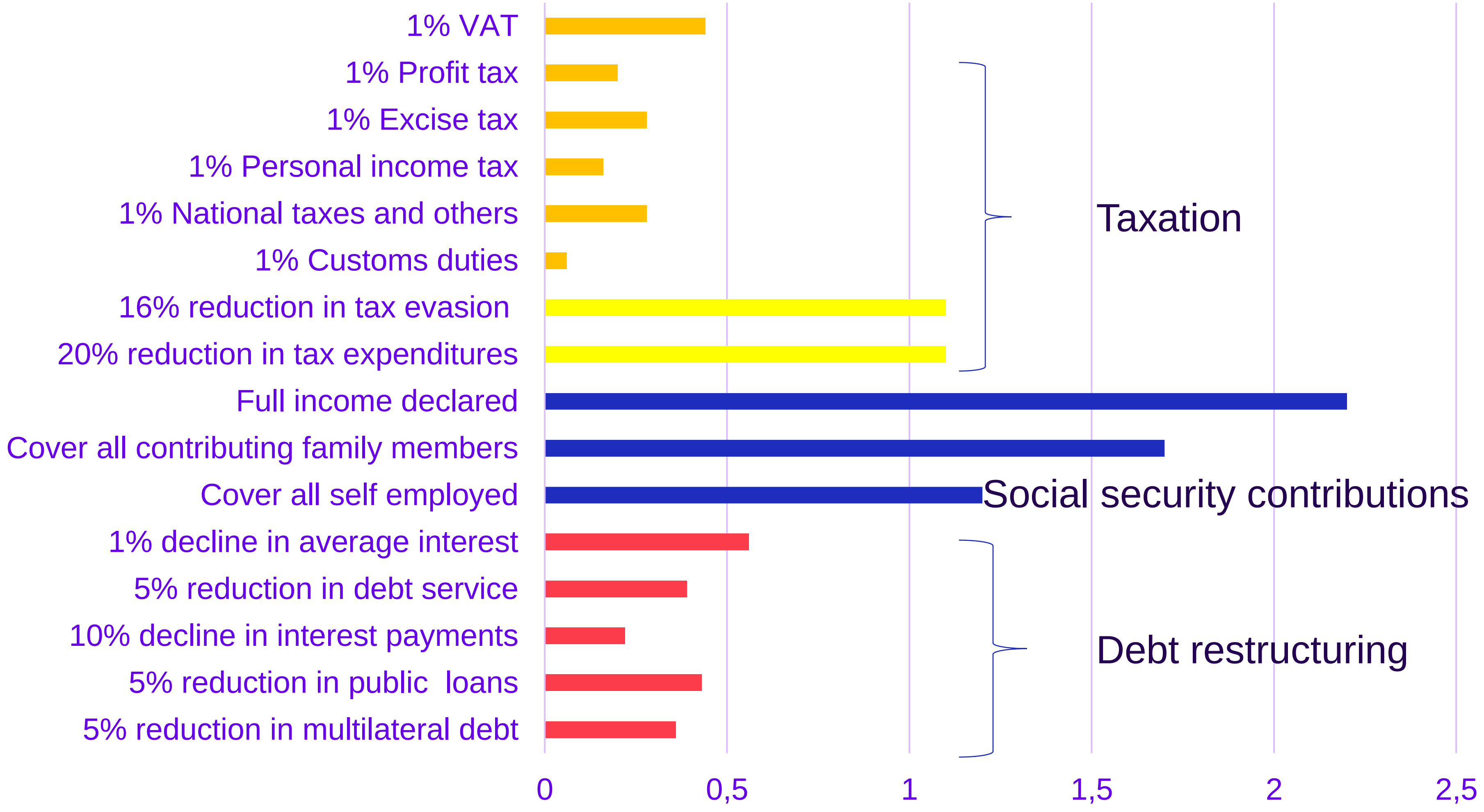


Debt restructuring

Estimated additional resources from debt related policy targets



Fiscal space options for Albania (% GDP)



Fiscal space options for Albania (4)

Other options to create fiscal space

1. A 20% reduction in illicit financial flows could generate between **0.23 – 0.58** per cent of GDP.
2. 20% of the reserves in excess under the most restrictive scenario could generate **0.40** per cent of GDP.
3. A more accommodative macroeconomic policy by setting fiscal deficits at 2 per cent of GDP could generate about **0.40** per cent of GDP.
4. Expenditure reprioritization has a very limited scope of creating additional resources for financing social protection.

Comparative final table

Table 7. Financing options and resource generation

Macro-category	Scenario	% of GDP
Expanding social security coverage and contributory revenues	Universal coverage of workers	5.8
Increasing tax revenue	VAT, additional 1 %-point	0.44
	Profit Tax	0.20
	Excise Tax	0.28
	Personal Income Tax	0.16
	National Taxes and others	0.28
	Customs Duties	0.06
	16% reduction in tax evasion	1.10
	20% reduction in tax expenditures	1.10
Eliminating illicit financial flows	20% reduction of illicit flows	0.23–0.58
Public expenditure reprioritization	10% re-prioritization of general public services and order safety recent gains in the budget structure	0.05
Use of fiscal and foreign exchange reserves	20% of the reserves in excess under the most restricted scenario	0.4
Debt restructuring	1-point decline in the average cost of the Albanian debt	0.56
	5% reduction in the debt service	0.39
	10% decline in the interest payments	0.22
	5% reduction in the public and publicly guaranteed (PPG) loans with IDA and IBRD	0.43
	5% reduction in the multilateral debt	0.36
Adopting a more accommodative macroeconomic policy	Set fiscal deficit at 2% of GDP	0.40

Source: ILO staff estimates using data from the IMF, World Bank, and national authorities.

Albanian woman. © Albania-the-Mirror.

Observations and lessons learned so far

- First attempt to quantify possible fiscal options to create fiscal space for social protection.
- More useful for the central government than local municipalities
- Reiterated the challenges of the existing system, e.g. low spending, high informality.
- Useful instruments to motivate and navigate the policy discussion with quantitative information.
- Need to build a consensus based on a national dialogue by all stakeholders.