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How to cover the time risk?

Response to Prof. dr. Lieve de Lathouwer

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Just five years ago, many countries were interested in how the welfare state was organized in the Netherlands. The 'Dutch miracle' was widely debated. However, I'm afraid that the Dutch miracle is dead and buried - if it ever existed, that is. The question now is can we learn from welfare state policies in other countries, for example in Belgium? Professor De Lathouwers's paper is very interesting and informative in this respect. It presents both a theoretical analysis of the so-called new social risks, and discusses the Belgian experiences with leave schemes.

I agree with the basic idea of the paper that time, or more specifically an appropriate balance between work and private life, can be considered as a new social risk that requires new institutional answers. For many people, the spread of work and other activities over the life course is far from optimal. At the same time, life course and work patterns are changing rapidly. I also agree that a life-course scheme that improves the balance between work and other activities - such as learning or caring for children or other relatives - may have benefits at several levels: the individual level, the level of the firm and the public level. Society obviously has an interest in time spent on good care for children and on life-long learning. It has often been stressed that modern welfare states should put more emphasis on such investments in human capital. Because of the benefits at several levels, shared responsibility for time arrangements seems to be the logical answer.

I have three comments on the paper. A central question is: what is the optimal time arrangement and what is the optimal collectivity to organize such an arrangement? The paper presents several arguments in favour of a basic public time insurance in the first pillar. The problem, however, is that new social risks are mainly manufactured or endogenous risks, which are difficult to insure. There is an obvious danger of moral

hazard. More specifically, it is plausible that a public time insurance will lead to a reduction in labour supply. And, if I understand it correctly, that is precisely what is happening with the Belgian time insurance, which to some extent functions as an early exit route and reduces employment rates. In this sense, the arrangement leads to the writing off of human capital, rather than an investment in it.

In my opinion, the challenge is to develop schemes that offer more opportunities to spread time for various activities over the life course on the one hand, while on the other hand maintaining or even improving the incentives for labour force participation. On this point, the economic view is that a savings scheme scores better than a public insurance. After all, periods of non-participation will lead to a decrease in savings and thus a decrease in future income, which will stimulate people to start working again. I admit, however, that a strictly individual savings scheme has serious drawbacks as professor De Lathouwer rightly argues: these drawbacks are problems of accessibility, transferability, gender inequality and a lack of solidarity. But these problems can be dealt with if an adequate mix of responsibilities is chosen. That mix may be the build-up of individual rights in a collective setting in the second pillar, with contributions from employers and with adequate tax support (for example through tax credits) to reflect the public benefits and to make the arrangement more attractive for large groups, including lower-income households.¹ The collectivity – for each collective labour agreement or sector of industry - makes it possible to introduce solidarity elements and offers economies of scale. The life-course saving scheme to be introduced in the Netherlands has some features of this model, but the scheme is not yet attractive enough for many employees. Nevertheless, it may be an interesting start for the further modernization of the welfare state. By integrating the life course scheme with the unemployment and pension schemes, the efficiency of the system might be improved. Several authors have recently argued that the introduction of integrated social savings accounts would contribute to the sustainability of the welfare state.² By applying these savings accounts on top of a basic level of social insurance, a better combination of solidarity and efficiency may be realized.

¹ This idea is elaborated by Leijnse et al (2002); see F. Leijnse, K. Goudswaard, J. Plantenga and J.P. van den Toren, 'A different attitude to security: life courses, risk and responsibility', Ministry of Social Affairs and Employment, The Hague, 2002.

² See for example A.L. Bovenberg and P.B. Sorensen (2004), 'Improving the equity-efficiency trade-off: mandatory savings accounts for social insurance', *International Tax and Public Finance*, 11(4), 507-529, S. Fölster (2001), 'An evaluation of social insurance savings accounts', *Public Finance and Management*, 1(4), 420-448 and J. Stiglitz and J. Yun (2002), 'Integration of UI with retirement insurance', NBER Working Paper no. 9199.

A second point is: should a life-course scheme be conditional or unconditional? It appears that the support in Belgium for thematic leaves is much stronger than the support for unconditional interruption of labour force participation. That is understandable, because there are few reasons to subsidize long holidays in the Bahamas (although such a trip might contribute to better health and higher productivity). There are good arguments to differentiate government tax support or subsidies between various activities; for example, higher support for parental leave with obvious public benefits, than for a sabbatical, where the private benefits are relatively higher. Also, the 'care risk' is of a different nature than the 'skill risk'. On the other hand, conditional leave and differentiation of government subsidies makes a life-course scheme more complicated. For example, how people spend their time has to be verified. Also, the freedom of choice of employees is reduced by conditional arrangements. This is a difficult dilemma, but it seems to me that some conditionality and differentiation in government subsidies cannot be avoided.

My final point concerns the distributional effects of a life-course scheme. Professor De Lathouwer argues that a time insurance in the first pillar has the highest potential for interpersonal redistribution. Theoretically this is right. But her analysis of the redistributive outcomes of the Belgian leave scheme shows that career breakers who benefit from the programme often have a relatively high income. In this sense, the time insurance does not seem to have the desired redistributive impact. On the other hand, I would argue that interpersonal redistribution does not have to be a primary goal of a life-course scheme. Instead, it should lead to a more equal distribution of income *over time*, that is, over the life course³. This point can be illustrated by the following example. Many households face a drop in their income when they are having children, just at a moment when income is most needed. This is the so called 'family dip'. An adequate life-course scheme should help to mitigate this dip. Next to a more optimal distribution of work and other activities, a life-course scheme should be directed at a more optimal distribution of

³ Interesting recent research by CPB Netherlands analyses redistributive effects of government programs on a life time basis; see H. ter Reeke, 'Measuring lifetime redistribution in Dutch collective arrangements', CPB Document no 79, The Hague, 2005. One of the conclusions is that income inequality when measured over the full life cycle is significantly smaller than inequality of annual incomes.

income over time. Again, social savings accounts – in combination with a borrowing facility⁴ – seem to be the logical instrument to smooth income over the life course.

⁴ A borrowing facility may be needed because for example some young parents will not have been able to save enough to finance their periods of (unpaid) leave.