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## **Belgian social federalism: Quo Vadis ?**

**Bea Cantillon**

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# **Belgian social federalism: Quo Vadis ?**

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## **Foreword**

This is one of a series of papers prepared in the context of our second 'conversation', funded by the Economic and Social Research Council (ESRC), on issues related to possible constitutional change in Scotland. These 'conversations' are being jointly organised by the DHI and Professor Charlie Jeffery of the University of Edinburgh. Professor Jeffery is also a Trustee of the Institute.

The first in the series covered macro-economic policy issues and financial sector oversight and regulation. The excellent papers from that conversation are available on our website. The third 'conversation' is to be on energy sector issues, in conjunction with the Scottish Council for Development and Industry (SCDI); and the fourth on competition policy and regulation, for which we have the full support of the Scottish Government. All four will be completed by end May 2013.

In each case our approach has been to commission papers from informed parties, then run a round table with key players. After the round table we ask authors to re-visit their papers, to be published on line at the time of a full DHI seminar, open to all.

This second 'conversation' covers issues related to social security and welfare under alternative constitutional settlements. We have received papers from; David Bell, Derek Birrell and Ann Marie Gray, Bea Cantillon, Nicola McEwen, Ailsa McKay, and Jeremy Purvis.

These are all now available on our web site. Taken together they provide a remarkably stimulating and wide-ranging assessment of the key issues and options - including informed input on experience outwith GB.

Our round table was held at the Royal Society of Edinburgh on 11 December 2012 and the full seminar is on Monday 19th February, again at the RSE. In addition to our authors' inputs, we arranged that Professor James Mitchell of the University of Strathclyde would sum up issues at the end of the round table and then set proceedings underway - in a constructive direction - at the seminar.

As with the other 'conversations' we have agreed with our friends at Scotland's Futures Forum that there should be a further round table, this time with MSPs in the autumn.

My Trustees and I are extremely grateful to the ESRC and the Binks Trust for their support; to Charlie Jeffery for organising the 'conversation'; to James Mitchell for his crucial input; and to all of our excellent group of authors. Together we believe we have made an important, evidence-based, informed and transparent contribution to this important topic within the context of the critical debate in Scotland on possible constitutional change.

At the same time, however, the DHI, as a charity, can have no views on these issues and hence I must record that the views expressed in this and the related papers are those of the authors and not of the Institute. Nevertheless we commend them to your attention.

Jeremy Peat  
Director, David Hume Institute  
February 2013

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## 1 Introduction

How can a bipolar and heterogeneous federation reconcile devolution of powers in the field of social security with safeguarding solidarity? For the negotiators of the sixth Belgian state reform following a regime crisis and a painful federal government formation which took one year and a half, this was one of the most difficult policy puzzles they faced.

Income redistribution that is realised through the mechanisms of social security is interpersonal in nature, from the healthy to the sick, from the employed to the incapacitated, from youngsters to the elderly, from rich to poor. Mechanisms of horizontal, vertical and intergenerational solidarity generate income redistribution between individuals facing different risks and income situations. Hence social security is, much more than taxation, an extremely important instrument to guarantee fundamental social rights, to redistribute income and to combat poverty.

To the degree that a) social risks are spatially unequally divided and/or the regional capacity to contribute to social security schemes varies, systems of inter-personal redistribution produces financial flows between regions in a country on the basis of capacity (wages) and needs (social risks). This makes social security the instrument *par excellence* to homogenise socio-economic differences in a country. With the insurance technique (enlightened self-interest) and built-in solidarity mechanisms, social security organises interregional income transfers which are automatically correcting for (regional) shifts in capacity and needs, for example caused by diverging ageing rates. For the first time in the (so far) six sequel long state reforms, the negotiators in 2011 could not ignore the question how social security (accounting for about 70% of total expenditure of the federal government and social security taken together) must be integrated in the Belgian layered policy structures. The previous state reforms had already unconditionally transferred important social powers and their associated resources to the Communities and Regions. However, extending the same splitting logic to the interpersonal transfer system of social security is much more difficult, not only – as we will see later – because of the different interests on both sides of the language border, the special position of Brussels, European law and the complexity of the systems, but also and especially because, as mentioned, the delicate balances that have been established in the social security system between insurance and solidarity are so important for the realisation of individuals' fundamental social rights. As splitting parts of social security entails a narrowing of the solidarity circle, worse social protection is looming, first for those who live and/or work in the least fortunate regions, and later – due to mechanisms of downward social and fiscal competition – possibly also for the more fortunate in the prosperous regions.

*Redistribution by social security is best organised at the highest possible level:* interregional transfers avoid unwanted competition between regions that could lead to social dumping, while expanded 'risk pooling' can better resist the consequences of economic and demographic shocks. That is the reason why in all welfare states (also in big and heterogeneous countries such as the US, Canada, Australia and Germany) the most important inter-personal solidarity streams are established at the highest national level. So, opting for federalism implies the organization of social security at the federal tier. The reason is that social security enhances both social and economic cohesion, crucial for the stability of federal states. Moreover, social security programs are important instruments of nation-building (Banting 2005) crucial to social cohesion. They are obviously important for the maintenance of the economic and monetary union and hence for the creation of economic cohesion.

Most importantly, while Flanders has the financial resources and fiscal capacity to pursue its own social security, the same is certainly not the case for the other sub-states ( Cantillon, 2011 ).<sup>1</sup>

But, for reasons of efficiency, legitimacy and durability inter-personal (and the resulting interregional) transfers should *neither* be caused by policy (or non-policy) in one particular region, *nor* deprive these regions of the necessary space to develop policy that is required by the local possibilities, necessities and preferences, *nor* lead to policy deadlocks due to the existence diverging political preferences in the constituting regions.<sup>2</sup> Moreover, in an asymmetric bipolar federal state, regional redistributive systems run into problems of legitimacy. While it is more difficult to find support for solidarity and redistribution at the more heterogeneous federal tier compared to more homogeneous sub-national tiers (Pauly 1973; see for a nuanced picture Jeffrey 2011), bipolar asymmetry and legitimacy deficiencies reduce the willingness to show solidarity. The maintenance of a major federal system of social protection therefore enhances pleas for confederalism. From this follows that recognising the (Flemish) striving for decentralization of matters related to social security is of vital importance to secure legitimacy.

So, nor splitting, nor the status quo of a centralised social security system – i.e. exclusive powers either for the regions or for the federal state - were therefore viable options for the future of Belgian social security. There was a strong case to be made for the principal redistributive instruments of social security to continue to be organised at the highest tier of government. At the same time, however, there were good reasons to argue in favour of greater powers for sub-national entities. The construction of a layered system of social protection, with shared powers where appropriate, therefore imposed itself.

How did the negotiators of the sixth Belgian state reform unravel this puzzle? Which were the driving rationales? And to which type of social federalism will this lead? This paper starts with a short repetition of the arguments in the debate on the devolution of social security. In a second part we recall the causes that led to the Belgian stalemate. In part three we look at the ‘rationales’ that have been used in the difficult pre-coalition negotiations. In part four we attempt to identify the main orientations in the provisions of the “Butterfly agreement”. Part five concludes.

## **2 On which tier should social security be organised? A short repetition of the theoretical arguments**

Economic literature on federalism and social redistribution cites *economies of scale*, *risk sharing* and *avoiding negative spill-over effects* as important arguments in favour of centrally organised systems of redistribution.<sup>3</sup>

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<sup>1</sup> In this respect, Watts (2008) rightly notes that the absolute size of a constituent unit affects the range of functions that they have the capacity to perform. For all these reasons, important powers in the field of social security must remain federal.

<sup>3</sup> D. Begg, J. Crémer, J.-P. Danthine, J. Edwards, V. Grilli, D. J. Neven, P. Seabright, H.W. Sinn, A.J. Venables en Ch. Wyplosz (1993), *Making Sense of Subsidiarity: How Much Centralization for Europe?*, London: Centre for Economic Policy Research.

Another classical argument states that social redistribution comes under pressure when it is organised at a lower tier of government and this due to the *mobility of labour and capital*.<sup>4</sup> In the classic *The Price of Federalism*, Peterson (1995) argues that decentralisation of redistributive policy forces regions (or countries) to ‘compete with each other’.<sup>5</sup> Regions (or countries) will be inclined to compromise on social benefits to reduce taxation pressure in order to attract the highly skilled and companies: “in a society where both people and business are highly mobile, it makes little sense to leave the marginal cost of welfare provision to lower tiers of government” (Peterson, 1995). According to the theory of fiscal federalism social redistribution belongs to a higher (supra)national level. Lower tiers can better concentrate on economic development policy such as education, infrastructure and safety. Belgium approximates this ideal: the federal government redistributes through one central income tax system, one social security system and by co-financing assistance. The regions or (sub)states concentrate on expenses for education and economic development.<sup>6</sup>

However, considered generally and more specifically from the Belgian context a couple of important reservations need to be made about these classical economic insights.

First, a critical factor in these theories is the *mobility presumption*. The less mobile employees and companies are, the smaller the danger for social dumping. Because mobility in Belgium is rather limited, the threat of negative social competition must be qualified.<sup>7</sup> Moreover, the history of welfare states teaches us that in large federations socio-economic *heterogeneity* (with rich and poor states) and the existence of many political ‘checks and balances’ have had a delaying effect on the development of systems of social redistribution. From this perspective, the simple observation of the post-war development of European welfare states compared with what took place in the US leads to a second qualification of the above mentioned (probably somewhat one-sided) economic assumptions. Based on the argument of fiscal competition Roosevelt in the US chose for a national social security system. Europe did not: intellectually supported by a report which argued that the risk for social dumping would be averted by strong unions and political majorities and hence did not seem to outweigh the advantages of competition, international trade and consequent economic growth,<sup>8</sup> the original six member states explicitly chose for *social subsidiarity*. Despite the theoretical assumptions, the European systems of redistribution effectively knew a much stronger development: much more than was the case in the US, economic growth in

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<sup>4</sup> C. Tiebout, C. (1956), ‘A Pure Theory of Local Expenditure’, *Journal of Political Economy*, 64: 5, p. 416-424; W.E. Oates (1972), *Fiscal Federalism*. New York: Harcourt Brace Jovanovich; W.E. Oates (1999), ‘An Essay on Fiscal Federalism’, *Journal of Economic Literature*, 37: 3, 1120-1149; D.E. Wildasin (1991), ‘Income redistribution in a common labour market’, *American Economic Review*, 81: 4, 757-774; D.E. Wildasin (1994), ‘Public pensions in the EU: migration incentives and impacts’ in A. Panagariya, P.R. Portney, R. Schwab (eds.), *Environmental Economics and Public Policy: Essays in honour of Wallace E. Oates*. Cheltenham, UK: Edward Edgar Publishers, Ltd; P.E. Peterson (1995), *The Price of Federalism*. Washington, D.C.: The Brookings Institution.

<sup>5</sup> P.E. Peterson, n. 6.

<sup>6</sup> Europe does the exact opposite.

<sup>7</sup> Still this argument must be taken seriously. First, because not only actual migration but also the political perception of the consequences of migration movements that ‘could possibly take place’ are of importance. A regional government for example, will be quite reluctant to provide higher unemployment benefits due to the fear that this would attract the low skilled from a neighbouring region where benefits are lower. Second, the very specific situation of Brussels needs to be taken into account, where sizeable commuter migration actually takes place. Finally, there is also the important fact that about 16% of companies in Belgium have settlements in different regions.

<sup>8</sup> Ohlin-report (1956), *Les aspects sociaux de la coopération économique européenne*. Rapport d’un groupe d’experts, Bureau international du Travail, Genève.



Europe has been converted into more social security. One explanation for this is the fact that within the relatively small and homogeneous territories of the EU member states it seemed to be much easier to organise social redistribution. In the US in contrast, the development of social security has been hindered by veto-coalitions from the poorer Southern states that feared to lose their comparative advantages (i.e. their lower wages). On the basis of thorough case studies, Obinger et al. conclude that “federalism had a general inhibitory impact on welfare state consolidation in the early democratic federations” (p. 332). They nevertheless add immediately that “once consolidation was accomplished, cross-national differences in spending trajectories were a function of a range of factors including partisan control, policy legacy and continuing institutional effects” (p. 332).<sup>9</sup>

More recent literature also develops more nuanced arguments for more decentralisation of social policy.<sup>10</sup> It argues that regional differences in preferences and needs, an adequate information flow and the possibilities for innovation, cost saving and adequacy of policy plead for decentralisation.

Sub-national entities can have different demands regarding the level and kind of public goods and services. This can be the result of different *preferences* such as is the case for home care that is more popular in Flanders than in Wallonia. There can also be differences in objective *needs*. The older age structure of inactivity in Flanders resulted for example in special efforts for the elderly unemployed while in Wallonia the focus lay on younger unemployed people. In such cases decentralisation is more efficient.<sup>11</sup> Due to diverging preferences and possibilities and difficulties in reaching consensus at the federal tier concerning the content of policy, the implementation of new and the dismantling of old systems of social protection have proven difficult in Belgium.<sup>12</sup> At a lower level of government it is sometimes simpler to reach a consensus as well as to obtain legitimacy. Wallonia’s resistance to stricter unemployment policy has undoubtedly had a strong delaying effect on Belgium’s activation policy. Also in other fields, federal social security policy often suffers from immobility which is at least partly explained by one sub-state’s fear that reforms would bring a split up of the social security system closer (as could be the case with a fiscalisation of family allowances).

The second argument refers to homogeneity and *the willingness to show solidarity*. At a smaller scale the connection between people is stronger and at that level the willingness to show solidarity and to redistribute can be greater than when this happens in a bigger and more heterogeneous entity.<sup>13</sup> An important question however is whether *broad* solidarity needs to be given up for *deep* solidarity (and vice versa). Social redistribution in Europe is greater than in the US, probably also due to the fact that European welfare states are smaller and more homogeneous. But in Europe solidarity stops at the countries’ borders, while Americans show solidarity among each other.

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<sup>9</sup> H. Obinger, S. Leibfried & F. Castle, n. 2.

<sup>10</sup> See a.o. Boadway and Shah, n. 2; M.F. Ambrosanio & M. Bordignon (2006), ‘Normative versus positive theories of revenue assignments in federations’ in E. Ahmad & G. Brosio (2006), *Handbook of Fiscal Federalism*, Cheltenham, E. Elgar, 306-338 and J.D. Wilson (2006), ‘Tax competition in a federal setting’ in E. Ahmad & G. Brosio (2006), *Handbook of Fiscal Federalism*, Cheltenham, E. Elgar, 306-338.

<sup>11</sup> This argument however should not be generalised nor exaggerated. In Cantillon, Schokkaert & Pestieau (2009) we demonstrated that the big challenges of social security in the field of pensions, health care and child benefits are common for the entire country. These challenges are particularly big given the relatively low level of protection and the expected important cost increase as a consequence of ageing.

<sup>12</sup> See for an overview of the theoretical arguments E. Ahmad & G. Brosio, n. 12.

<sup>13</sup> M.V. Pauly (1973), ‘Income Redistribution as a Local Public Good’, *Journal of Public Economics*, 2: February, p. 35-58.

Some authors therefore argue that national solidarity will also decrease to make pan-European solidarity possible: “if the EU is ever going to be a more uniform ‘land of opportunity’ for the citizens of all of its member states, where terms like social cohesion and solidarity do not stop at each country’s border but encompass all EU citizens, we expect that the common denominator of EU-wide social institutions will become more like those in the United States”<sup>14</sup>.

Conversely, in this line of reasoning one could say that a relative decrease of *interregional* solidarity in Belgium will give wings to *intraregional* solidarity. The Flemish care insurance could be considered as a case in point: precisely in a period in which social security expenses needed to be kept under control and reducing the fiscal and parafiscal pressure had become an important policy goal, Flemish parliament succeeded in introducing a new social contribution and this on the basis of a very broad consensus.

The third argument refers to *innovation*.<sup>15</sup> Decentralised policy can provide more space for innovation. Experiments at a lower tier are less risky and easier to implement. It has for example been demonstrated that after decentralisation of Spanish policy many regions have demonstrated a large degree of policy innovation.<sup>16</sup> Moreno and Trelles conclude that “the greater the need for innovation (for example a ‘new’ problem or solution), the greater is the rationale for that function to be provided by the sub-state government”.<sup>17</sup> In Flanders the care insurance could serve as an example of innovation.

Empirical reality offers many indications of the advantages of decentralisation. The most developed welfare states in Scandinavia are not only characterised by homogeneity and a small scale approach but also by a high degree of decentralisation of implementation.

For reasons of enlightened self-interest but also and mainly because the socio-economically weaker regions in Belgium (namely Wallonia and Brussels) are structurally dependent on income transfers to keep the welfare model afloat, important redistribution streams must remain organised at the federal tier. Solidarity between communities (in the generic sense) can however be organised in different ways, be it through interpersonal solidarity (such as social security and taxation), be it by interregional/state transfers (such as allocations/grants).<sup>18</sup> We will argue later why we think that in a general and theoretical sense interpersonal solidarity is superior to interregional transfers. But in practice trade-offs must be made, keeping into account popular support, efficiency considerations and historic opportunities. It is for example unlikely that Europe will be able to organise interpersonal solidarity like the US does within the foreseeable future. Project financing (as organised by the Social Funds) or interstate transfers are more probable. In the Belgian context, the efficiency gains to be expected from a homogenisation of elderly care policy may justify a conversion from interpersonal to interregional solidarity.

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<sup>14</sup> R.V. Burkhauser & K.A. Couch (2010), ‘Are the inequality and mobility trends of the United States in the European Union’s Future?’ in J. Alber & N. Gilbert (eds.), *United in Diversity? Comparing Social Models in Europe and America*. Oxford University Press, 305.

<sup>15</sup> W.E. Oates, n. 6, 1120-1149.

<sup>16</sup> J. Subirats (2005), ‘Social Exclusion and Devolution among Spanish Autonomous Communities’, *Regional and Federal Studies*, 15: 4, 471-483.

<sup>17</sup> L. Moreno, en C. Trelles (2005), ‘Decentralization and Welfare Reform in Andalusia’, *Regional and Federal Studies*, 15: 4, 519-535.

<sup>18</sup> When we argue (along with others) that reducing solidarity means a decline of civilisation we mean solidarity in a general sense, not the instruments to organise this solidarity.

This overview of the pros and cons of decentralisation teaches us that nuanced thinking is at its place. From the viewpoint of social adequacy (*which system offers the best guarantees for the best possible social protection for as many people as possible*) social redistribution is better organised at the highest possible tier of government. At the same time considerations of political legitimacy, efficiency and innovative potential need to be taken into account. The right *balance between broad and deep solidarity* is not a given, but depends on the phase of social systems of redistribution as well as on numerous contextual parameters.

### 3 What preceded the sixth state reform

At the negotiations of the sixth state reform the pressure to transfer important powers in the field of social security to the Communities had become very strong, and this not only for obvious political reasons on which we shall not dwell here. Previous transfers of so-called ‘person related matters’ in the field of health care and assistance to persons, towards the communities and economic powers with among others placement services and elements of labour market policy towards the regions, inevitably caused border conflicts with federal social security<sup>19</sup> which resulted not only in ever louder calls for so-called ‘homogeneous power packages’ but also in a growing need for ‘accountability’ of sub-national entities for the consequences of their policy for federal social security.<sup>20</sup> Additionally, the evolution of social security policy itself, just as in other countries, gave way to increasing pressure to decentralise: the relatively new focus on activation and ‘empowerment’ requires tailored policy which is best organised at lower tiers of government.<sup>21</sup>

On 3 March 1999, Flemish parliament approved five resolutions in which Flemish parties advanced a common position in preparation of a new state reform, with as focal points regional labour regulations, partial fiscal autonomy, and partial regionalisation of social security among others in the field of health care and child benefits. Thereby, the following principles applied: more *coherent packages of powers*, *duality* on the basis of two sub-states (with in addition Brussels and the German Community), *maintaining solidarity* on the basis of objective and transparent mechanisms and *cooperation* between authorities.

The subsequent declarations to revise the constitution however, offered few prospects for the realisation of these resolutions. That is why Flanders tried to force its way into social powers through a ‘creative’ implementation of the powers it already had at its disposal. The Flemish care insurance was a first test case that despite objections of the Legislation Section of the Council of State, has passed constitutional review for the largest and most fundamental part.<sup>22</sup>

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<sup>19</sup> We refer for example to the BAMA (Bachelor-Master) reform and the choice for a different duration of the master programmes at both sides of the language border which affects expenditure in the sector of child benefits.

<sup>20</sup> The term ‘accountability’ is interpreted in very different ways in public discourse, see on this subject among others Vandenbroucke en Meert, 2010; we come back to this issue later.

<sup>21</sup> See for example Y. Kazepov & E. Barberis (2012, forthcoming), ‘Social Assistance Governance in Europe. Towards a Multi-level Perspective’ in I. Marx & K. Nelson (eds.), *Minimum Income Protection in Flux*. Basingstoke: Palgrave Macmillan.

<sup>22</sup> See J. Velaers (2010), ‘Het sociaal federalisme in België in het licht van de bevoegdheidsverdeling’ in B. Cantillon, P. Popelier & N. Mussche (eds.), *De gelaagde welvaartsstaat*. Antwerp: Intersentia.

The Constitutional Court's case law gave wings to the Flemish aspirations for its own social policy, outside of any state reform and hence without having to negotiate with the French language community. The Flemish coalition agreement<sup>23</sup> declared in 2009 the prospect of 'a basic decree related to Flemish social protection' which would among others involve a basic hospitalisation insurance and a financial allowance for children.<sup>24</sup>

The experience with the Flemish care insurance has been very instructive.<sup>25</sup> First, it became clear that the development of the existing constitutional setting of 'exclusive powers' took place in a 'legally uncertain' manner with numerous legal procedures at the Council of State, the Constitutional Court and the European Court of Justice as a consequence.<sup>26</sup> Second, the 'case by case' exaction of Flemish social powers threatens to result in a policy architecture with little coherence. The Flemish care Insurance for instance, was at least in part introduced on the basis of the motive of establishing Flemish powers in the field of social security. The same took place later when a Flemish child benefit was worked out.<sup>27</sup> Obviously this is not the right starting point for the development of adequate social policy. Likewise, it became clear (moreover not only in the case of the care insurance) how an uncontrolled 'race to the top' in social protection threatened to arise: when sub-national entities introduced new policy instruments the federal tier was inclined to react to this in order to safeguard its own role in social security. We witnessed both in the care sector as well as with child benefits elements of a cost increasing dynamic that is obviously hard to justify in a period of major budgetary difficulties. Third, hardly any stimuli existed for any coordination between policies of the different tiers of government, quite on the contrary.

It was clear that Belgium faced a dangerous vicious circle. Immobility at the federal tier strengthened Flemish aspirations for more regional autonomy. But conversely, the Flemish attempts to establish own social powers were partly responsible for blocking the necessary modernisation of federal social security. Caught within the logic of the principle of exclusivity the French speaking side reacted time after time by initiating legal proceedings at the Constitutional Court and the European Court of justice. Out of fear of loss of powers obvious reforms were also being obstructed. For instance the fear of a possible loss of powers proved a not insubstantial obstacle to the necessary simplification of the system of child benefits, among other things. We nevertheless need to mention that the threat of a possible split of social security stimulated Wallonia to eliminate the so-called 'inexplicable differences' in health care. There are reasons to presume that the same took place in the field of active labour market policy.

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<sup>23</sup> Flemish coalition agreement 2009-2014 of 9 July 2009, *Een daadkrachtig Vlaanderen in beslissende tijden. Voor een vernieuwende, duurzame en warme samenleving*, p. 67. See also coalition declaration of the Flemish government, *Parl.St.* VI. Parl. 2009, 31/1, 6.

<sup>24</sup> See on this issue J. Vanpraet (2010), 'Naar een Vlaamse sociale bescherming binnen het bestaande bevoegdheidsverdelend kader' in B. Cantillon, B., P. Popelier & N. Mussche, n. 25.

<sup>25</sup> See for an extensive analysis B. Cantillon, P. Popelier & N. Mussche, n. 25.

<sup>26</sup> See a.o. J. Velaers (2010), '[Het sociaal federalisme in België in het licht van de bevoegdheidsverdeling](#)' in B. Cantillon, P. Popelier & N. Mussche, n. 25; J. Vanpraet (2010), 'Naar een Vlaamse sociale bescherming binnen het bestaande bevoegdheidsverdelend kader' in B. Cantillon, P. Popelier & N. Mussche, n. 25; P. Popelier (2010), 'Sociaal federalisme en bevoegdheidsverdeling in rechtsvergelijkend perspectief' in B. Cantillon, P. Popelier & N. Mussche, n. 25.

<sup>27</sup> Making benefits conditional upon the services of *Kind en Gezin* (child health and development centres) is undoubtedly inspired by the concern to make a legal distinction with federal child benefits: 'The benefit, that is independent of child benefits, is only paid if parents have their children monitored preventively by *Kind en Gezin* or by an equivalent set of paediatricians and GPs.'

## **4 The sixth state reform and Belgian social security : four ambiguous premises**

The negotiators of the sixth state reform assumed four ‘captive’ premises and rationales: (i) splitting (parts of) social security while (ii) maintaining solidarity through interregional transfers, (iii) creating so-called homogeneous packages of power, and (iv) rendering the sub-national entities accountable. These four ‘rationales’ however, are all ambiguous, they run into conceptual misunderstandings and/or practical problems and they are mutually not always consistent. This undoubtedly partly explains why the negotiations that led to the sixth state reform took so long and why the resulting political compromise resulted in a very hybrid outcome.

### ***4.1 Why mature systems of social protection are difficult to split : the particular nature of social security schemes***

For the first time in the process of Belgian state reform, the question of how to integrate social security in the Belgian layered government structure could not be ignored. The previous state reforms had already unconditionally transferred important social powers and their associated resources to the Communities and Regions. However, extending the same splitting logic to the interpersonal transfer system of social security is much more difficult, mainly because of the nature of the system itself.

#### *4.1.1 The complex nature of social security (schemes)*

A developed and mature social protection system as Belgian social security has a complex institutional and financial architecture (mainly socio-professionally organised and financed), relies on complex governance structures (involving employers organisations and trade unions) and consequently requires considerable expertise in its implementation. It is hard to disentangle and transferring competences fully to sub-national entities is an expensive and politically (cf. infra) risky operation that requires a vast investment, time and moneywise. To take the Belgian system of child benefits as an illustrative example : the systems includes 3 different schemes (for employees, for the self-employed, for civil servants), each one is financed in its own way, with its own very complicated entitlement rules and benefits that are intertwined with other benefits (such as unemployment benefits) and are also linked with, among others, the tax system.

#### *4.1.2 Social security and its basic principles*

##### *4.1.2.1 Social security as an instrument of solidarity*

Social security in Belgium was originally set up as an instrument of interpersonal solidarity mainly based on horizontal and to a lesser extent on vertical and intergenerational redistribution. Yet, Belgian social security has also become an important instrument of interregional redistribution. It reduces regional income inequality by about 60% and hence is an important instrument of federal homogenisation. It operates in a transparent and flexible way in function of the changes in the spatial distribution of ‘social risks’ and ‘contribution capacities’.

The Butterfly agreement explicitly starts from the principles of national solidarity and interpersonal redistribution.<sup>28</sup> These principles are guarded by a) keeping replacement incomes with the strongest potential for redistribution federal and b) keeping funding of the powers to be transferred federal (governed by the finance act). For the parts of social security that are transferred to the regions the resources are distributed through federal grants, based on a demographic allocation formula. In fact this means that it is presumed that a similar degree of solidarity can be organised by means of interregional transfers with (potentially conditional) allocations. Moreover, it is also presumed that *interregional transfers* would be ‘more transparent’ than transfers through social security. But are both presumptions correct?

As mentioned before, for the parts of social security that are transferred, the inter-personal solidarity logic will not apply anymore but rather gives way to interregional solidarity through allocations with demographic allocation formulae. Even though these criteria are meant to take into account the evolution of needs it is clear that they will only do so to a limited degree. The interpersonal redistribution of social security automatically corrects for (regional) shifts in capacity (wages) and needs (due to for example a different ageing rate in the regions concerned; relative changes in morbidity and birth rate; schooling; structural and cyclical shifts on the labour market, etc.). An interregional transfer ideally would take the same factors into account. In case of means tested benefits for assistance to the elderly for instance, the criteria do not take into account the evolution of the share of low income families in a region and in case of child benefits the share of families that are entitled to increased benefits is ignored. This means that the extent of solidarity between rich and poor regions will decrease. Moreover, it would be very difficult, if not impossible to detect the mentioned shifts on time to be able to integrate them in some sort of ‘allocation model’ for distributing budgets across the sub-states. The statistical apparatus and awareness of possibly relevant divergences in socio-demographic and economic trends indeed always lag behind social reality. From this perspective, social security does organise a transparent and flexible regional redistribution on the basis of a commonly accepted ‘contribution basis’ and ‘social risks’.<sup>29</sup> We will further see that trading interpersonal for interregional solidarity as anticipated in the ‘Butterfly agreement’ – certainly in case of child benefits and labour market policy – is not neutral *precisely because an already very complicated allocation system cannot take into account the many factors that determine the needs and capacity of sub-states.*<sup>22</sup>

In addition, interregional solidarity in Belgium will have to be enforced in a battle between the weaker ‘them’ (Wallonia and Brussels) and the stronger ‘we’ (Flanders). It is unlikely that the result of this process will be equally generous as solidarity generated by insurance and enlightened self-interest: “... thinking explicitly about interregional solidarity, focuses attention on regional identities. Would this help in keeping the interregional solidarity intact? ... Feelings of a shared fate are not only necessary for creating strong social insurance institutions, they are also influenced by the existing institutions. The remaining feelings of a common understanding in Belgium are certainly influenced by the mere fact that we now have federal social insurance institutions in place.

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<sup>28</sup> ‘No sub-state may impoverish structurally’ and ‘its (of the federal state) fiscal prerogatives related to interpersonal redistribution policy should stay intact’.

<sup>29</sup> See also for this argument E. Schokkaert & C. Van de Voorde (2007), ‘Defederalisering van de Belgische gezondheidszorg?’ *Leuvense Economische Standpunten* 2007/119, May.

Breaking up these institutions would bring us in the longer run in the EU or in the world situation”.<sup>30</sup> Therefore, trading interpersonal for interregional solidarity almost inevitably means a *less ‘broad’ solidarity* in practice.

Finally, as the resources are not pegged to a rise in GDP (in case of child benefits the allocations increase only with inflation and in case of the other powers to be transferred, except for hospital financing, with 82.5% of real growth of per capita GDP) also an important *inter-temporal brake* has been built into *interregional solidarity*. In view of the costs of ageing and the expenditure increase in the past<sup>31</sup> it is clear that allocation growth foreseen for elderly care as a whole will not suffice and hence that the sub-states will have to chip in or will have to reduce the existing level of protection. The same applies to child benefits. This also means that a mechanism is triggered through which Belgian social federalism will ever more evolve to a *‘shared cost federalism’*<sup>32</sup> with built-in cost control at the level of federal government expenditure.

Summarizing, after the sixth state reform the largest and more important streams of solidarity remain inter-personal and federal. Yet, Child benefits and Allowances for Assistance to the Elderly will be split and interpersonal solidarity will be traded for – less generous – interregional solidarity. This means that solidarity will become less broad. It is unsure to what extent this will - in the long run - be accompanied by a deeper solidarity within smaller sub-national entities but also how the allocated federal grants will evolve over time.

#### 4.1.2.2 A farewell to Bismarck?

The way the parts of social security that are transferred to the regions are financed (through federal grants) after the sixth state reform will have two additional implications. First, for a Bismarckian system such as the Belgian one, the link between social benefits and social contributions is cut<sup>33</sup> and an *important structural reform* is initiated from a socio-professional contribution related system to a *universal system financed from general funds*.<sup>34</sup>

#### 4.1.2.3 Workplace versus residence principle

Second, in contrast to national social security – where the workplace principle (the insured opens rights in the place where he works) applies, the defederalised parts will necessarily apply the residence principle (social rights arise at the place of residence). In case of a strong intertwining with federal social security (as for example is the case with child benefits where increased benefits are linked to the beneficiary’s social status or as is the case for policies for target groups) obviously a set of new coordination rules will need to be developed and introduced.

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<sup>30</sup> E. Schokkaert (2009), *Trust and social insurance*. Re-Bel E-book 1: ‘On the interaction between subsidiarity and interpersonal solidarity’.

<sup>31</sup> Since 2000 the sector of care for the elderly grew annually by an average of 7.5% (without inflation), CM p. 13.

<sup>32</sup> H. Obinger, S. Leibfried & F. Castles, n. 2.

<sup>33</sup> At the same time the issue arises on the involvement of the social partners in the management and implementation of the parts of social security that will be transferred.

<sup>34</sup> The reform towards a so-called two pillar system has been part of subsequent reform plans for many years, see among others R. Dillemans (1993), *Bouwstenen voor een nieuwe sociale zekerheid*. Leuven: Universitaire Pers Leuven. Before powers are transferred, the systems of employees, the self-employed and civil servants must be aligned. This is a complex but necessary exercise that will contribute to a very important simplification.

### 4.1.3 *Brussels*

Although Belgium is most often referred to as a bipolar federal model, a third player should be taken into consideration when reorganising social security territorially. If competing Flemish and Walloon social security systems would be introduced in Brussels, a system must be found to assign all its residents objectively to one or the other system. Either a form of sub-nationality is required (Flemings, Walloons and newcomers would have to commit themselves and their children more or less permanently to one or the other community and its accompanying system) or it has to be accepted that a separate social security system is developed for Brussels<sup>35</sup>. In that case the architecture of Belgian social federalism must become threefold. The second option is however problematic due to the scale and the exceptionally large asymmetry in risks and contribution capacity in Brussels. The strong concentration of a socio-economically weak population and hence of social risks in Belgium's capital goes hand in hand with great prosperity and hence contribution capacity that is, however, generated by commuters.

Second, Belgium faces the difficult problem of Brussels. Social security is not just another insurance. It is a social insurance: it is affordable for weaker groups because the stronger groups contribute more than they actually should from a sheer insurance technical point of view. That is why social insurances do not tolerate freedom of choice. Insurers are not allowed to make a distinction between good and bad risks and the insured cannot choose for the system that suits them best. If competing Flemish and Walloon social security would exist in Brussels a system must be found to assign all Brussels residents objectively to one or the other system. This requires a form of sub-nationality: Flemings, Walloons and newcomers would have to commit themselves and their children more or less permanently to one or the other community and its accompanying system. If one wants to avoid this, there is no other option than to accept that a separate social security system is developed for Brussels (in the end this solution was chosen through the Common Community Commission (COCOM), see below). In that case the architecture of Belgian social federalism must become threefold. What's more, a transfer of powers to the Regions is problematic due to the scale and the exceptionally large asymmetry in risks and contribution capacity in Brussels: the strong concentration of a socio-economically weak population and hence of social risks in Belgium's capital goes hand in hand with great prosperity and hence contribution capacity that is, however, generated by commuters.

### 4.1.4 *The international regulatory framework*

The wider international regulatory framework imposes limitations to a different territorial organization of social security. E.g. the limiting European rules on free movement of workers should be taken into account. If entitlements – as is necessarily the case when designing sub-national social security systems – are tied to residence, the residence principle will inevitably clash with the workplace principle that currently governs the entire body of entitlement rules in social security and is also used by European law on the subject.

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<sup>35</sup> This is the solution that was actually chosen – in a hybrid form – by transferring powers on child benefits and Allowances for Assistance to the Elderly to the Common Community Commission (COCOM).



#### **4.2 The fiction of homogeneous policy packages : towards an ‘intertwining’ of powers**

Traditional discourse on institutional reform often refers to the necessity to create ‘homogeneous power packages’. Even though there are good examples of inefficient distributions of powers it is an illusion to think that in increasingly layered social policy it is possible to achieve homogeneity: numerous limitations exist that are imposed by the broader international framework and there inevitably is a strong entanglement of different policy domains (such as social benefits, taxation, work, education, family and care).

The Belgian sixth state reform, however, has added little ‘homogeneity’. The ‘Butterfly agreement’ provides a ‘homogeneous’ transfer of powers in the field of elderly policy. However, the transfer of powers concerning labour market policy, health care and child benefits result in a (further) ‘intertwining’ of powers regarding social security.

First, this will require more cooperation and coordination and if successful this could lead to a form of ‘joint decision federalism’ in which the federal government and social partners *together with* communities and regions will shape social security policy. The need for cooperation is confirmed in several domains, including the domain of social policy. Interesting in this respect is the plan to establish an inter-federal institute for health care (p. 38). Also, the coalition agreement provides for the conclusion of cooperation agreements (p. 41-42).

*Second*, the sub-national entities will be dependent on the federal administrations for the implementation of their policies. This leads to a ‘shared implementation federalism’. The National Social Security Office as well as the National Employment Office (for labour market policy) and the National Health Insurance Office (for health care) remain the sole administrative and technical operators.<sup>36</sup> At least in the transition phase (which will take long in view of the complexity of the operation) the Communities will also remain dependent on the administrations that pay the child benefits.<sup>37</sup> This administrative intertwining can, if successful, lead to a strengthened *common interest* and ditto legitimacy with all entities that will be responsible for guaranteeing fundamental social rights to citizens.

#### **4.3 Accountability versus autonomy**

The third and most recently surfaced rationale for rearranging powers in the field of social security is ‘accountability’. This principle has been interpreted in various ways, from ‘autonomy’ (a split system of own resources and within homogeneous powers is the best guarantee that regions spend their resources efficiently) to ‘accountability to the whole’.

In the case of social security<sup>38</sup> the first interpretation of accountability obviously runs into the above mentioned obstacles of splitting and homogenisation of power packages. *Fundamentally, autonomy cannot be detrimental to general interest nor stimulate the sub-national entities to design policies that are detrimental to other sub-national entities.*

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<sup>36</sup> It is moreover not improbable that the National Child Benefit Office will remain the administration for child benefits for Brussels in view of the fact that the scale of Brussels is too small to set up its own administration. The power for structural reductions in social security contributions and the exemption from remitting withholding tax remain federal.

<sup>37</sup> Literature on federalism considers administrative cooperation as a feature of cooperation federalism (see among others H. Obinger, S. Leibfried & F. Castles, n. 2, 263 on Germany and Switzerland).

<sup>38</sup> For a discussion of macro accountability elements in the finance act we refer to A. Decoster in P. Popelier, D. Sinardet, J. Velaers & B. Cantillon (eds.), *België, quo vadis? Waarheen na de zesde staatshervorming?* Antwerp, Intersentia.

It must for example be avoided that a sub-national entity develops policies that aim to attract the highly educated at the cost of other sub-national entities.

The second interpretation is more recent. The argument goes that when sub-national entities exert a real influence in the framework of their powers on the expenses of federal social security, shared financial responsibility and impulses to design policies that benefit *general interest* result in efficiency gains. As sub-states are competent for social policy as a whole, except for social security, and as they also draw divergent policy paths, this more and more becomes a critical factor of the adequacy of federal social security (see for example activation policy, prevention policy in health care and education policy).

The idea that with forms of accountability it would be possible ‘to preserve Belgian solidarity while favouring efficiency’<sup>39</sup> enjoys quite some intellectual and political support. However, the proposals were quite rudimentary and remained silent on their practical implementation. Dewatripont therefore rightly warned that ‘God is in the details’. Rendering sub-national entities accountable with a bonus malus system indeed runs into the great difficulty of finding relevant assessment criteria: cyclical unemployment for example, is determined by factors that lie outside of the influence of federal as well as of regional policy.<sup>40</sup> Imposing a malus for substandard regional performance moreover runs into the objection that it could cause a downward spiral whereby in times of rising unemployment and hence of an increased need for activation, the resources to do so would decrease.<sup>41</sup>

In the previous section we indicated that recently a certain convergence took place around the idea of rendering the regions more accountable for federal social security by means of financial (des)incentives. The sixth state reform however does not contain elements of accountability *in that sense of the word*, nor in the sector of health care, neither in the sector of labour market policy.<sup>42</sup> This can probably be explained by the difficulties mentioned earlier to define parameters that should and should be able to support such accountability policy.

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<sup>39</sup> M. Dewatripont (2009), A comment on Marcourt and Vandenbroucke’s call for action in the interest of economic recovery and social progress. Re-Bel e-book 2: ‘Does it make sense to regionalize labour market institutions?’.

<sup>40</sup> P. Van Rompuy (2008), ‘Werkloosheidsverzekering in een federale staat met een toepassing op België’, in B. Cantillon & V. De Maesschalck, n. 4.

<sup>41</sup> In the course of pre-formation discussions, a concrete accountability proposal was put on the table, written by Vandenbroucke, that aimed to render the regions accountable on the basis of their labour market performance. It proposed to give the regions that catch up on their labour market performance a financial surplus on a temporary basis. Vandenbroucke’s proposal aimed to support the regions with input funding by giving them 10.000 euro for every permanently activated unemployed person. See among others B. Van der Linden (2008), ‘Quelles réformes pour nos institutions du marché du travail ? Réflexions autour d’un certain nombre de pistes’, in B. Cantillon & V. De Maesschalck, n.4.

<sup>42</sup> In the sector of child benefits, the demographic allocation formula (the evolution of the share of minus 18 year olds) could be read as an incentive to avoid any extension of study duration. Even though in child benefits policy freedom is most extensive (depending on the stipulation that will be included in the constitution, the sub-national entities will even be able to use the resources of child benefits for other purposes, for example for the development of child care) the demographic allocation formula contains an additional element of accountability: by using the age limit of 18, the communities are stimulated to design higher education policy that discourages any extension of study duration as much as possible. Moreover, due to the delayed (and in the case of child benefits the total lack of any) coupling to GDP growth, the entities are compelled to contribute to their own parts of social security.

In health care as well as in labour market policy it is indeed not self-evident to find a clear link between policy input and output: to questions such as ‘to what degree do actions in the prevention sphere have an influence on health expenses?’ or ‘how big is the net result of various forms of activation?’ no scientific consensus exists, let alone that a political consensus could be reached in the matter.

As was the case in the past, communities and regions are awarded the full spending authority over the transferred funds. Hence, these will be unconditional.<sup>43</sup> Sub-national entities will be able to ‘*spend*’ the transferred budget ‘(including possible surpluses ) as they please’ for various forms of labour market policy in the broad sense of the word (measures concerning labour costs, education and monitoring of job seekers, employment programs, ...), for elderly care and for child benefits.

Hence, there are no traces of direct forms of accountability through the above mentioned bonus malus systems. Does this mean that the new distribution of powers cannot lead to greater accountability and more efficiency? Obviously not, spending freedom entails that the sub-national entities ‘will feel the consequences of their actions (or their policy) themselves’ (Vandenbroucke, 2011). If for instance they develop successful employment policies that decrease the number of ‘target groups’ for which reductions in social contributions are necessary, they will be able to use the resources that are made available for this purpose for other policy purposes.

As mentioned before however, ‘accountability through autonomy’ should not yield any danger for public interest or for another sub-nationality. As it is clear (for reasons explained in section 2) that unemployment insurance must remain a federal matter, one will have to make sure that sanction policies maintain a certain degree of homogeneity. Also, cooperation agreements will have to be concluded regarding the intensity of monitoring the unemployed. It is indeed clear that a common social insurance can only exist with (relatively) homogeneous implementation rules. Also concerning tax reductions, agreements will have to be reached to avoid overly divergent wage calculations for companies with Walloon, Flemish and/or Brussels employees. If successful, this will lead to shared responsibilities and more cooperation between the Belgian sub-national entities .

## 5 Belgian social federalism after the sixth state reform

The negotiators of the sixth state reform started from four ‘captive’ rationales: (i) splitting (parts of) social security, (ii) creating so-called homogeneous power packages, (iii) maintaining solidarity through interregional transfers and (iv) rendering the sub-states accountable. We demonstrated that these ‘rationales’ are ambiguous and run into important conceptual misunderstandings and/or practical problems. Moreover, they are mutually not always consistent. Hence, it should not surprise that the concluded agreement is hybrid in nature. The largest and more important streams of solidarity remain *inter-personal* and federal. Child benefits and Allowances for Assistance to the Elderly will be *split* and interpersonal solidarity will be traded for – less generous – interregional solidarity. This means that solidarity will become *less broad*. This *can* be accompanied by a *deeper* solidarity within smaller sub-national entities. However, there is no certainty on the issue.

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<sup>43</sup> “The specific allocations for Brussels amount to 363 million euro in 2030 and must be spent for about half of it on specific goals such as mobility, safety and urban development. In that sense these allocations are a first in Belgian federalism. They are an example of *conditional* allocations that up until now were absent in our system (see De Coster & Sas, *o.c.*).

A *homogeneous* transfer of elderly policy is anticipated but at the same time on quite some topics a further ‘intertwining’ of powers will take place. Some important levers of employment policy will be transferred in view of rendering sub-states *accountable* even though there are no direct (des)incentives to induce the communities and regions to design policy that favours ‘general interest’. Regions and communities will penetrate some decision making bodies of the federal social security system and many coordination platforms are anticipated to strengthen *cooperation* in a landscape that will undoubtedly become much more complex.

Taken as a whole we think we can argue that the sixth state reform will move Belgium in the direction of a social federalism with a) *shared costs*, b) *shared decisions* and c) *shared implementation*. In a bi-polar, by definition non-hierarchical system, this holds great dangers: ‘shared’ in this setting means de facto veto-rights.<sup>44</sup> If however the transferred powers are handled responsibly, and the social partners retain an important role in the systems’ management, and moreover the constitutional court takes a strong stance in the protection of fundamental social rights, it is not impossible that a basis will develop on which a durable and inclusive layered system of social security could develop.

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<sup>44</sup> See on this topic Frank Vandenbroucke’s reaction on our plea for a layered, dynamic system with shared, concurrent and competing powers (B. Cantillon, P. Popelier, & N. Mussche, n. 25): “*That is the fundamental Cantillon dilemma: to make shared powers a concept that is both productive and stabilizing, you need hierarchy of norms, which we do not have and will not have for the foreseeable future*” (F. Vandenbroucke, <http://www.rethinkingbelgium.eu/rebel-initiative-ebooks/ebook-9>).

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