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Gloomy Prospects for Social Retirement Insurance

An International Phenomenon

by Karl Heinz Jüttemeier, Hans-Georg Petersen, Kiel*

Recently, important experts have presented two studies concerning the current situation and future prospects of social retirement insurance in the Federal Republic of Germany.¹ Now there is also an internationally comparative study on the same subject available.² The German co-authors summarize the results of that study and add some proposals for further discussion.

During the last decade the social retirement systems of more and more Western countries were confronted with increasing financial difficulties. In public these problems are mainly seen and discussed under short-term, i. e. business cycle, aspects; but gradually more people are becoming aware of the fact that there exist some long-term, i. e. structural, deficiencies which are much more dangerous and might even be able to threaten today's system as a whole. Thus, the system which to a great extent represents that which is known as the "social progress of the 20th century" has to undergo changes.

So far, however, the history of public retirement insurance schemes seems to be a rather unique report of success. Originally, they were founded as a mandatory system of precautionary measures which a paternalistic state provided in order to protect its blue-collar working classes against poverty in old age. During the 1930s and 1940s social retirement systems began to incorporate the majority of white-collar employees and in the 1950s and 1960s they have even grown to cover almost everyone. In most of the industrialised countries transfer payments from social retirement insurances now constitute the most important, if not the sole source of income for the elderly.

Further common features characterizing the development of social insurance schemes in industrialised countries are:

□ During their initial phase they followed in principle the normal pattern of every private life insurance company,

i. e. they were organized as funded systems. Thus, there existed a close connection between contributions paid by the active insurees and their future pensions; but unlike private companies no adverse selection took place and individual risk factors were disregarded. Consequently, redistributive effects were already incorporated from the very beginning, being at that time, however, of minor significance.

□ The second phase saw a fundamental change of the financing system. Apart from Japan, most social retirement systems left actuarial funding and turned to pay-as-you-go financing. This conversion occurred in the United States as early as in 1939, only a few years after its social security system was founded, whereas the European countries mainly switched to pay-as-you-go financing after World War II.

□ Finally, the close correlation between contribution payments and future benefits was dissolved, e. g. by introducing minimum pensions (Japan, France, Italy, Great Britain) or by calculating them according to minimum incomes (FR Germany), by taking into account only years with the highest active incomes (France, Great Britain), or by decreasing the retirement age without actuarially adjusting individual pensions (for

¹ Cf. Transfer-Enquête-Kommission: Das Transfer-system in der Bundesrepublik Deutschland, Stuttgart, Mainz 1981; Deutscher Bundestag, Gutachten der Wissenschaftlergruppe des Sozialbeirats zu längerfristigen Entwicklungsperspektiven der Rentenversicherung, Bundestagdrucksache 9/632, 3. 7. 1981, cited in the following as "Sozialbeirat".

² Cf. Jean-Jacques Rosa (ed.): The World Crisis in Social Security, Fondation Nationale d'Economie Politique and Institute for Contemporary Studies, Paris, San Francisco 1982.

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instance, the option of earlier retirement age, i. e. the flexible retirement age in FR Germany). All these measures led to a strong increase of redistributive elements within the social retirement systems.

Some further common characteristics can be seen in the fact that in nearly all countries females seem to be favoured by earlier retirement ages and – likewise a world-wide phenomenon – that public employees (government officials) have pension entitlements usually considerably exceeding the replacement rate (average benefit relative to average salary) of private sector employees. Italy seems to be at the top: if one joins the Italian public services at the age of 20, males can retire at the age of 40 and women at the age of 35 (if married or with children); then their replacement rate amounts to 60 %.³ In France government officials as well as employees of the nationalized industries get comparatively higher pension payments; resulting deficits of these special systems are borne by the general social retirement system.⁴ In the Federal Republic of Germany pension levels for government officials are considerably higher than those arising from the general social pension scheme.

Apart from problems depending upon an individual country's specific regulations for its social retirement system, there are two important common factors which have caused the increasing financial difficulties. Firstly, the elasticity of the expenditure side of the social insurance budgets is – not only in the short run – considerably higher than that of the revenue side and, secondly, the population is aging and the age structure will deteriorate even more rapidly in the decades ahead. In other words, the increasing deficits (or decreasing surpluses) will have increasingly structural causes.

For a better understanding of the effects on the social retirement insurance scheme, one has to visualize the main elements of the two possible financing procedures. Somewhat simplified, the alternative methods can be described as follows: in a funded system expenditure is a function of revenue (because benefits are closely tied to contributions) and vice versa for a pay-as-you-go system. In the first case the size of contributions is contractually fixed and the later pension payment results from the accumulated fund and its compound interest accruing in the course of time; since the level of pension benefits is by no means fixed and can eventually also converge towards zero, deficits do

not occur. In the latter case, on the other hand, the levels of pension payments are politically fixed, i.e. a replacement rate which might depend on the active income, contribution period etc., is legally determined by a pension formula; deficits do not arise as long as contribution payments can be adjusted to meet the financial requirements. An increase in the contribution rate (or the payroll tax rate), however, is inevitable if the dependency ratio of aged persons (ratio of workers to retirees) is falling due to declining fertility or higher pensions are provided resulting from a politically initiated rise in the replacement rate.

Most politicians engaging in social policy seem to prefer pay-as-you-go financing systems. This is quite understandable since from their point of view this method is doubtless more pleasing: the introduction of redistributive measures can be very easily implemented within the pension formula without burdening in the short-run the contributing insurees with perceptible financial burdens. This was especially true under the prevailing post-war conditions of most industrialised countries. A growing population and an annual increase of productivity even gave the false impression that pay-as-you-go financing is the cheaper procedure, since under such circumstances even a constant contribution rate (related to a continuously growing assessment basis) always led to higher revenues. Thus, room for redistributive manoeuvres seemed to open up which the politicians have used excessively for improvement in benefits. As a result, each insuree contributed less to the system than he got back as pension payment because those benefits were borne by a larger and/or more productive generation of employees. During this phase of development the respective generation of retirees absorbed "windfall profits" and the politicians made their "political gains". But this kind of mishandling the pay-as-you-go financing method by one-sidedly passing on surpluses in the form of improved benefits sooner or later must lead to deficits or growing contribution rates. Now when the population is starting to decrease and growth rates are declining or even negative the redemption of the unpaid bill from the sixties and seventies is becoming more and more difficult.

Deteriorating Dependency Ratios

In particular, the foreseeable demographic developments will soon require a reform of the benefit structure; otherwise contribution rates will have to rise to a level which is today completely unimaginable. All industrialised countries forecast that their dependency ratio of aged persons will greatly deteriorate and that the ratio of workers to retirees will reach 2.0 or – depending

³ Cf. Onorato Costellino: Italy, in: Jean-Jacques Rosa (ed.), op. cit., p. 51.

⁴ Cf. Jean-Jacques Rosa: France, in: Jean-Jacques Rosa (ed.), *ibid.*

on the assumptions regarding future birth rates – might even fall considerably below this ratio.⁵ Presuming today's benefit levels and a future economic growth rate of 2 or 3 %, it is expected that, for instance,

□ in the United States an increase in the payroll tax rate (including the employer's contributions) from about 10 % today to more than 26 % will be necessary;⁶

□ in Japan, which forecasts a dramatic increase in the dependency ratio of aged persons, the ratio of contributors to beneficiaries will decline from 8.2 in 1980 to 1.6 in 2025. But even under the Japanese funded system the contribution rate will have to increase from 10.6 % to 16.0 %. In the case of a pay-as-you-go financing system Japan today would have a contribution rate of only 5.5 %, but then would have to increase the rate to 30 % or more by 2025;⁷

□ in the Federal Republic of Germany a doubling of today's contribution rates will be necessary;⁸

□ in Sweden the contribution rate might rise to 24 % in 2020 which means more than double the 1980 rate.⁹

⁵ In the Federal Republic of Germany most prognoses indicate that in 2030 the ratio of workers to retirees will be 1.2 : 1 and, pensions of government officials included, perhaps 1 : 1. Cf. Hans-Georg Petersen: *Sicherheit der Renten? Die Zukunft der Altersversorgung*, in: *Hintergründe*, Vol. 4, pp. 135, Würzburg, Wien 1981.

⁶ Cf. Sherwin Rosen: United States, in: Jean-Jacques Rosa (ed.), op. cit., p. 152.

⁷ Cf. Noriyuki Takayama: Japan, in: Jean-Jacques Rosa (ed.), *ibid.*, pp. 77.

⁸ Cf. Helmut Meinhold: *Ökonomische Probleme der sozialen Sicherheit*, Kieler Vorträge, N. S., Vol. 86, Kiel 1978.

The social policy which was applied worldwide during recent years did not see, or did not want to see, the long-term financial consequences. Thus, on the expenditure side generous benefit regulations were introduced without paying sufficient attention to the long-term financial requirements. For the German retirement insurance, for instance, huge surpluses were forecast which then were actually distributed in the 1972 reform. The big mistake everywhere consisted in the fact that politicians reacted to fluctuations in the status of liquidity asymmetrically: revenue surpluses were used for improvements in benefits whereas financial bottlenecks in the liquidity situation were taken as a chance to increase the contribution rates. As a result, the once close link between individual contributions and individual pension payments was weakened further. It seems to be a matter of fact that governments pay more attention to immediate issues which instantly provide for political benefits during the next election campaign. In this respect, the pay-as-you-go financing rule literally does not set up any obstacles preventing politicians' short-sighted exploitation of the rule.

Basic Social Security Rates

The table compares the basic social security rates for the countries in this study. In considering these figures, it is important to recognize their limitations, since it is almost impossible to give an exhaustive description of all structural provisions determining social retirement

⁹ Cf. Ingemar Ståhl: Sweden, in: Jean-Jacques Rosa (ed.), op. cit., pp. 107.

Comparison of Basic Social Security Rates

Country	Earnings test	Contribution rate (%)			General revenue	Share of GNP (%)		Replacement Rate (%)	
		Basic	Supplemental	Ceiling (\$ 1,000) ^a		Basic	Supplemental	Basic	Supplemental
France	No	12.9	—	10.5	—	7.65	—	41.9	—
FR Germany	Yes	18.5	—	22.0	14	11.2	—	47.0(m) 37.5(f)	—
Great Britain	Yes	20.45 ^b	—	16.0	15	5.5 ^c	—	23.0	25.0
Italy	Yes	24.2	—	—	13	12.0	—	30.0/80.0 ^d	—
Japan	Yes	10.6(m) 8.9(f)	— ^e	22.0	20	3.76	—	45.0 ^f 42.0/100.0 ^f	combined
Sweden	Yes	8.4	12.25	—	—	6.2 ^g	3.3 ^g	60.0	combined
Switzerland	No	8.4	6.4	— ^h	16	5.8	4.1	50/150 ^{h,i}	combined
United States	Yes	12.26	—	29.7	—	12.8	—	45.0	—

Key: (f) female, (m) male.

^a Dollar value based on exchange rates of 1 July 1981. ^b The British rate is 7 % less for those who choose to contract out of the government system.

^c Private retirement insurance of those who contract out equals another 5 % of GNP. ^d Replacement rate in Italy ranges from 30 % up to 80 %.

^e Japan's tax rate includes both basic and supplemental insurance. ^f Average replacement rate in Japan is 45 %. Japan's richest pensioners receive 42 %; the poorest receive more than 100 %. ^g Medical portion of Swedish social security is 5 % of GNP. ^h In Switzerland, the supplementary programme is undergoing revision, which is expected to levy about 15 % on incomes between \$ 8,200 and \$ 24,600 per year. In the basic programme, there will continue to be no ceiling. ⁱ For couples with incomes between \$ 3,600 and \$ 21,800.

Source: J. J. Rosa, A. L. Chickering: A political dilemma, in: J. J. Rosa (ed.): *The World Crisis in Social Security*, Paris, San Francisco 1982, p. 219.

insurances in individual countries. Pension levels for most countries fall in the range of 40 to 50 % (replacement rate); only two countries, Sweden and Italy, exceed this range. And since in all countries benefits are related to contributions, at least to some extent, it is not surprising that replacement rates positively correlate with contribution rates, thus again showing Sweden and Italy at the top of the scale. However, some countries transfer additional funds from general revenues to their social security systems. Taking these into account, too, the cross-country comparison reveals that especially the British and German systems seem to be quite "expensive" ones: average levels of replacement rates go along with high levels of contribution rates plus a substantial transfer rate from general budgets. In the case of the United Kingdom it should be added that its pension system combines a network of private occupational pension schemes with a comparable state scheme.¹⁰

Shift into the Underground Economy

In most industrialised countries public pension insurances are today already facing severe financial stress and will do so all the more when the projected changes in the population's age structure come into effect. Current social policy, however, still carries on on the basis of the principles established during the initial phase, disregarding the differences between today's situation and that of the initial position as well as changes in the insurees' behavioural patterns which have occurred since then. The success of old age security, especially that provided by social retirement insurance, has led to the result that the equation "pensioner depending mainly or totally on social security means poverty" is becoming more and more dubious.¹¹ But, nevertheless, even such entitlements to benefits which originally were meant to cover only really poor groups of pensioners are now accessible to larger sections of the population. With the best of intentions to solve the problems of a few, politicians introduced general regulations and now they look surprised that the legal entitlements thus constituted are claimed in general, possibly even by those wealthy retirees whose individual level of income does not at all demand any kind of socially motivated protection. Politicians of nearly all countries are lamenting quite a lot about this spreading attitude of moral hazard concerning social security benefits. But their response resembles rather a tragicomic attempt to criminalize such behavioural patterns by tightening up existing laws or introducing

new and complicated regulations which mostly show themselves to be inefficient but add to the system's complexity – an optimal prerequisite for moral hazard. But does it really make sense to blame the recipients which, living in a market-oriented environment, show economically rational reactions towards the social security system?

Too much altruism is demanded if the single citizen is asked to voluntarily disclaim the benefits arising from advantageous regulations which his neighbour possibly already receives. Thus, for instance, in Germany hardly anyone renounces the extremely favourable option for an earlier retirement age being financed by all active insurees, because those perhaps willing to work longer would be discriminated and be called fools in public. It is not the citizen who failed, but politics: perpetuating old political goals by never analyzing if and to what extent they are already achieved, and exercising justice by taking into account everyone and everything, inevitably must lead to a complex social security system and in most countries also to a likewise complicated tax system. The different regulations and provisions for exceptions have become non-transparent and incomprehensible for the majority of people but exploitable for a minority. Thus the attempt to do justice to everyone rather produces injustice for a great many (*summa ius, summa iniuria*).

Sure, for a certain time politics can continue as if nothing is going to happen. But sooner or later demography will require heavy interventions in today's security systems; in fact, the stronger recessions and the lower future growth rates are, the sooner the need for intervention. Continuing to balance the inherent dynamics of the expenditure side by exclusively burdening working generations through tax rate increases, soon will take us to the limits of taxation: more and more employees will adopt new behavioural attitudes in order to evade additional burdens or even taxation altogether. Opportunities of evasion offer themselves through social welfare, early retirement, and the underground economy.

Some European countries should serve as a warning signal. In this respect the Italian example is rather illustrative and has already entered economic literature as "Italy's new economic miracle".¹² It is mostly agreed among experts that the growth of the Italian underground economy is to a large extent induced by the existing tax and transfer system, which, for instance, offers high replacement rates, earlier (flexible)

¹⁰ Cf. R. Hemming, J. A. Kay: Great Britain, in: Jean-Jacques Rosa (ed.), *ibid.*, pp. 29.

¹¹ Cf. Sozialbeirat, *op. cit.*, para. 9.

¹² Herbert Giersch: Comment on Paul Samuelson's Paper: The World Economy at Century's End, Kieler Arbeitspapier No. 110, Kiel 1980, p. 7.

retirement ages, generous criteria concerning disability, etc. Onorato Costellino states in his analysis: "Italy has superimposed a strong dose of Mediterranean light-heartedness."¹³ Nonetheless, the Italian economy still works well even in the form of a "workable anarchy", in contrast to many socialist countries in Eastern Europe which face similar tendencies towards an underground economy but are facing total bankruptcy.

In the Federal Republic of Germany, obvious preliminary symptoms of an underground economy can be seen. But the empirical evidence for a strong increase is not very impressive¹⁴ even though the marginal burdens of taxes and contributions on the working generation's incomes have reached top levels as compared to international standards. Probably, the speed of adaptations in behavioural attitudes also depends on the prevailing national mentalities and the threshold beyond which adjustments might occur massively differs from one nation to another. True, it is almost impossible to define objective limits of taxation but the present experience shows that today's subjectively felt limits already create big problems in financing public expenditure.¹⁵

The shift of economic activities from the official into the underground economy must not necessarily endanger current societies; some aspects may even have their positive effects on the further development of Western societies.¹⁶ In any case such a development certainly would contribute to a further deterioration of social retirement insurance schemes' financial status because revenues would decrease and, fixed replacement rates assumed, future deficits would increase.

Inherent Structural Deficiencies

Of course, the gloomy prospects of the social retirement systems do not lack some speculative elements; the underlying assumptions could well prove to be too pessimistic. Looked at today, it is often hard to imagine that fertility rates, or the rate of growth of the economy, might strongly increase again; in both cases financial problems would be less serious. However, the analysis clearly shows that the deficitary trend is caused primarily by the systems' inherent structural deficiencies. No matter how future developments may

actually come true, fundamental reforms of the existing social retirement insurance schemes are inevitable.

Modifications could be done on either the revenue or the expenditure side. Since today's contributions are already felt to be too high and further increases bear the great danger of strong disincentives for the working generations, reformatory efforts concentrate on reductions of social security benefits. The increasing of present retirement ages is probably the proposal most commonly preferred in international discussions.

The United States, for instance, is considering an upward adjustment of the retirement age from 65 to 70 while European countries seem to focus more on a model with flexible retirement ages which provides for an actuarial discount or bonus but leaves the individual free to fix the date of retirement. In the end both models do not show any great difference; in either case it will come to a relief of the expenditure side. Other proposals concern the methods of indexing benefits, a reduction of redistributive elements, etc.; most of these proposals are constructed according to an individual country's specific circumstances.

Economic growth and the dimension of expected financial problems are negatively correlated: the lower future growth rates the bigger financial difficulties will turn out to be. In this context some economists emphasize that social security systems per se may have retarding effects on growth. Especially some empirical studies done by Feldstein¹⁷ seem to suggest that today's pay-as-you-go financing has reduced private savings. Indeed, his ultra-rational life-cycle analyses allow for such conclusions but, on the other hand, the studies do not provide unequivocal evidence. The variables of the model are highly intercorrelated and the influence of social security can hardly be separated from other motives determining private savings behaviour. And developments in Germany also provide no evidence for his thesis. Although the country has very high rates of social security contributions its savings rates are among the highest in the Western world.

For contemporary social policy a switch from pay-as-you-go financing to a funded system – as is implied by the Feldstein studies – is of minor significance: in a phase characterized by a decreasing number of contributing insurees and an increasing number of pensioners, reserves cannot be built by a funded system either, because even the accumulated fund

¹³ Onorato Costellino, *op. cit.*, p. 56.

¹⁴ Cf. Hans-Georg Petersen: *Size of the Public Sector, Economic Growth and the Informal Economy. Development Trends in the Federal Republic of Germany*, in: *The Review of Income and Wealth*, Series 28, 1982, pp. 191.

¹⁵ Cf. Sozialbeirat, *op. cit.*, para. 171.

¹⁶ Cf. Hans-Georg Petersen: *Size of the Public Sector*, *op. cit.*

¹⁷ Cf. Martin Feldstein: *Social Security, Induced Retirement and Aggregate Capital Accumulation*, in: *Journal of Political Economy*, Vol. 82, 1974, pp. 905; Martin Feldstein: *Social Security*, in: Michael J. Boskin (ed.): *The Crisis in Social Security: Problems and Prospects*, Institute for Contemporary Studies, San Francisco 1979, pp. 17.

itself is needed to meet the current pension payments. Such is the situation in most industrialised countries and changing the financial rule in order to build up reserves would mean a strong increase in today's contribution rates, which would then all the more create disincentive effects. As things are, switching to a funded system would not solve financial problems; it is an unimportant alternative.

Partial Corrections or Total Turnabout?

In the Western economies there seems to be an implicit understanding among most political parties that social retirement systems have to be reformed but should not be abolished. However, in which way and to what extent such reforms have to be carried out is a matter of controversy: some people believe that a few partial corrections of undesired developments will be sufficient to safeguard social security systems in the long run, leaving the basic idea of a paternalistic system unchanged. Others think a reorientation of social policy to be necessary and propose a total turnabout, i. e. turning away from traditional principles and policy goals.

Partial repairs surely will reduce some of the current defects; however, the question remains whether or not they will be able to stabilize social security systems in the medium and long run. Probably not! As already discussed above there are three elements jeopardizing social security in the long run: (1) demographic development trends, (2) the high expenditure elasticity resulting from the present kind of benefit calculation, and (3) undesired, or rather unanticipated, behavioural adaptations by the insurees. Demographics belong to the basic data which for the retirement systems represent exogenous variables and can hardly be influenced. As opposed to this, expenditure performance and behavioural adaptations is a must.

In the past a great deal of social progress was obviously achieved, but at the same time a huge redistributive machinery came into operation which, according to public opinion, handles enormous sums while showing only small redistributive net effects. This raises general opposition which can hardly be overcome by linear cuts within the social security systems. As far as the Federal Republic of Germany is concerned the problems are of a structural kind. Linear cuts would be an inadequate method of abolishing existing undesirable trends: rather, they would prolong them, if not even lead to an aggravation. But if substantial reforms are necessary, towards which aims should they be directed? What is needed is a conception, a target to pursue; its formulation is politicians' primary task.

It is an easy matter to list dozens of objectives which the public associates with social security. The German Social Advisory Council (Sozialbeirat), for instance, specifies twelve main objectives, among others also "stability of matrimony and family, social mobility, avoidance of solitude".¹⁸ However, it seems to us that for the basic idea of any social retirement insurance there is in the end only one relevant objective and that is to secure incomes in periods of life during which individuals are no longer able to earn their living. In socially oriented economies this aim is more or less achieved if people do not have to worry about how to meet everyday material needs. If only basic protection should be provided, leaving higher levels of protection to individual choice, or if social security systems should go beyond this, is a matter of society's agreement. In the first case elements of an individual responsibility are emphasized while the second case accentuates more the paternalistic attitudes.

More Regard for Individual Preferences

100 years of social security policies and the coinciding great economic progress have brought about an important improvement in the standard of living for the vast majority of the population in the industrialized countries. People are no longer as poor, as uninformed, and as powerless as their ancestors once used to be. And to the extent that most employees' level of income and wealth has risen, the once great need for public compulsory protection has declined. Given these facts one should expect revisions of today's social retirement systems towards more flexibility with regard to individual preferences. Retirement systems just providing basic protection seem to be in a better position to take into account such considerations and they might even be better prepared to get over the expected long-term financial crisis. Some of the aspects of this will be discussed below.

Today's system of social retirement security is the outcome of a long historical process of development; often the schemes are very complex and consist of a variety of different kinds of insurance such as, for instance, mandatory public systems, supplementary public systems – some mandatory and some voluntary –, occupational systems organized on an intra- or inter-industry basis with regional or nationwide significance, voluntary individual insurance contracts some of which are tax privileged, and also social welfare payments. It is not astonishing that these complex systems do not follow one or two basic principles but rather form a conglomerate of many ideas, partly

¹⁸ Cf. Sozialbeirat, op. cit., para. 34.

contradicting each other. Thus the systems are far away from being rationally constructed: levels of replacement incomes, qualifying requirements, and methods of financing differ to a very large extent and, as a consequence, often different amounts of benefits are granted for identical factual situations. In particular, government officials' pensions are extremely privileged and other groups are able to cumulate benefits out of the different sections of an uncoordinated system. Therefore a harmonization should be aimed at in which the mandatory public systems could well be attributed the role of providing basic social security.

The benefits from such basic programmes must be indexed in order to guarantee a constant relative share of a socio-cultural minimum protection over time. Higher replacement rates exceeding minimum security should be left to individual responsibility and could well be assigned to supplementary programmes. As far as they are organized within the existing public systems they must strictly follow the principle of equivalence, i. e. benefits are granted according to contributions paid. But forms other than saving through insurance are also conceivable, and especially the possibility of individual wealth accumulation might gain greater significance as compared to the present. In any case, a restructured social retirement system which increases reliance on individual responsibility does not have to exert the pressure of moral suasion on the population's self-control in order to avoid an excessive exploitation of legal entitlements vis-à-vis anonymous public institutions.

Reform of the Tax System

However, harmonizing the social retirement schemes will not be possible without substantial reforms of today's tax system. The current financial crisis of public budgets should really be taken as a good chance to integrate most transfer payments into the system of income taxation. Thus the problems of cumulation benefits out of an uncoordinated tax and transfer system will diminish which, for instance, in Germany are giving rise to growing concern. Taking everything into account the introduction of a system of negative income taxation would probably be the best solution, at least one of the most bitter reproaches concerning today's huge redistribution machinery could be eliminated, that is, redistributing money only from the left-hand pocket to the right-hand pocket.

In spite of all difficulties, radical cuts in the existing social security systems could be avoided if the reorientation of social policy started in the near future. In fact, the sooner reforms are undertaken, the less severe

the burden of demographic and financial constraints will be; but the longer we wait, the more drastically contribution rate increases and/or benefit cuts will have to come into effect. There is still enough time left for a slow process of stepwise reforms, but, unfortunately, legislative authorities do not seem to be interested in spending much time on it. Thus it is not surprising that the political discussion on new long-term perspectives is still as badly needed as it is regrettably absent. It seems to us that the most crucial point is to encourage today's policy-makers and the public to take these issues seriously and act on them.

Demography, increasing moral hazard, and a growing underground economy will make a fair distribution of future burdens difficult if not even impossible. Unless social security benefits are reduced substantially or taxes and contributions are increased, the present system will collapse. Among these options, increasing taxes is not a viable alternative because high and rising taxes will also have seriously increasing disincentive effects; the other alternative is to reduce benefits. Somehow solutions must be found to safeguard the so-called "generation treaty" without imposing a hopeless burden on either current or future working generations. Perhaps politicians should call to mind what kind of prospects for the future are offered to young people: for the next ten years they will be confronted with high unemployment and, correspondingly, with restricted alternatives for training on the job, but at the same time during the next decade when their chances start to improve, the vast increase of expenditure for old-age security starts, too. Do we really believe that we can saddle every burden only on today's young generation?

Often, criticisms and the resulting proposals for new concepts are defamed by pressure groups as "social dismantling", but if we again try the old long-standing recipes, substantial social cutbacks will indeed be inevitable. It is high time to tell people that some of the traditional aims of social policy cannot survive in the long run and that it would be better to rely on one's own responsibility instead of trusting blindly in governments', politicians', bureaucrats' and pressure groups' capability of making the best of it. On the contrary, it seems more likely that informed individuals are better prepared to look further ahead than most politicians who – due to their limited terms of office – tend to pay more attention to immediate issues bringing immediate political gains. Unfortunately, in twenty or thirty years we can no longer call them to account for the damages: once the horse has bolted, it is too late to lock the stable door.