

# Social Security in Theory and Practice: An Essay <sup>\*</sup>

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Comments welcome.

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## ABSTRACT

Understanding the role and functions of social policy and social security systems is a key point for a discussion on reforms of the retirement systems. In this essay I describe the subject and range of social policy in the modern welfare state. The work has a descriptive character and aims at presenting basic issues between social security, social policy and social insurance. In the first part I provide a discussion on the welfare state's definition and its structure; then I refer to the notion of social policy and present ideological foundations for social security development. Also, a typology of social policy regimes is presented. The essay also deals with the concept of social security, discusses its definitions, origins and discusses development. I go over the discussion concerning classical assumptions underlying the social security concept and present some recent major challenges that make the review of social security construct necessary. Some terminology and institutional differences between the US and European framework are presented as well. Part three analyses the issue and origins of various risks faced by society. Those social risks are described along with the social risk management issues that are at heart of current approach to social policy. The last part shortly deals with the functions of social security with a focus on social insurance as its main tool.

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# Chapter 1 Social Security in Theory and Practice : an Essay.

## 1. Subject and range of social policy

### Introduction

Pensions and old-age protection issues are characterized by and firmly related to the concepts of welfare state and social policy. Socio-economic factors (mainly ideology, tradition and level of economic development) influence the way the welfare state is constructed and the scope of its social policy. Therefore, before starting any pension-related discussion, it seems essential to define these concepts, or at least try to outline their common meaning. I will also describe shortly their contents.

### Welfare state: definitions and structure

Barr (1992: 742) points out that it has been extremely difficult to define what actually “the welfare state” is and that even for some classics like Richard Titmuss, this term still represents an “indefinable abstraction” (Titmuss, 1968: 124). Barr (1992: 742) concludes that the term “welfare state” refers to four main state’s activities, that is: cash benefits; health care; education; and food, housing and other welfare activities (benefits in kind).

According to Briggs (1961), the welfare state is characterised as a state that exists for three main purposes: to guarantee to a family some minimal level of income, to provide some safety mechanisms against social risks (inability to gain income while sick or old) and to keep some equality concerning social service. Therefore, the welfare state is:

“a state in which organised power is deliberately used (through politics and administration) in an effort to modify the play of market forces in at least three directions – first, by guaranteeing individual families a minimum income irrespective of value of their work or property; second, by removing the extent of insecurity by enabling individuals and families to meet certain “social contingencies”... and third by ensuring that all citizens without distinction of status or class are offered the best standards available in relation to a certain agreed range of social services” (Briggs, 1961: 222 quoted in Harris (2000: 4)).

Harris himself describes the welfare state as an “overall network of support” (Harris, 2000: 4). A state can be referred to as *being* a welfare state or *having* a

welfare state. The second option seems to be applied for states with only “residual” welfare services; that is, the ones like USA or Japan that offer only some basic safety net (Harris, 2000: 5, italics in original).

There exists also a dual definition; either the welfare state is characterised by its functions or by its mechanisms (institutions and procedures) that are developed to achieve those functions (Mishra, 1984: chapter 1; quoted in Harris, 2000: 5).

The fundamental roles of modern state are much more than merely the basic state protection of individual rights (internal security achieved by law and police and external security created by national defence). In addition to this role, Holcombe (1999: 101) enumerates also: public production, regulation, redistribution and stabilization.

The welfare state can be therefore conceptualized in its strict (social goods and services, providing and organising social security systems) or wider version (expanded by non-budgetary actions of the state aimed at improving the social welfare, particularly by redistribution and regulation mechanisms like progressive taxes, minimum pensions, wages, or control of rents and prices).

The welfare state is undoubtedly an evolution of the State, a response to increasing demand for social economic safety yet (especially in its wider context) also a result of increased wealth of society and economic possibilities of developed states accomplished during decades of economic growth after the Second World War. Not surprisingly, the welfare state concept concerns mostly the well-developed countries. A particular example of this mechanism is Singapore – a well-being patrimonial state that has emerged from nothing within the lifetime of one generation.

I might thus think of the welfare state as a social institution (typical for developed countries) which produces, organises, distributes and regulates social goods and services (institutional dimension) and which is responsible for providing people with some commonly agreed level of those goods and services to protect families and individuals against social contingencies and to stabilize the socio-economic environment (functional dimension). This responsibility can be based on the citizenship notion (that is the state is responsible for well-being of its citizens) or more broadly on ethical grounds (the state should provide at least some basic level of protection to all its residents). The difference is not so trifling if we consider the globalization and unification tendencies (vide European Union) and the problem of immigrants or “Gastarbeiters”).

Each country has its own design and rules for welfare benefits; however one may

give a general outline as follows (Barr, 1998: 7-9). The social state benefits can come in cash or “in nature” (i.e. goods and services). The later concern mainly health protection, education and housing. Cash benefits cover two main categories. The first is social insurance related to benefits that are awarded regardless of wealth or income (means-tests) but on the basis of either previous contributions or a specified contingency (unemployment, marriage, reaching a specified age etc.). The second class includes non-contributory benefits (i.e. contributions are not required) that might come either in form of universal benefits granted on the basis of a specified contingency (but again, without means-testing) or social assistance conferred upon the basis of an income or wealth test. Social insurance includes therefore contributory reimbursements like: unemployment, sickness, disability benefits, retirement benefits (pensions) and non-contributory payments like: income support, other income-related benefits and child-related benefits.

The welfare state, as any other social institution in the area of economic policy, should serve three main objectives that Barr (1998: 9) describes as: efficiency, equity and administrative feasibility. This much for the “positive” part of the welfare state problematic; however as any social institution also the welfare state is adherently rooted in the ideological issues ranging from whether such an institution is needed at all to degrees of its size and rules of operation.

### **Definition and role of social policy**

Defining what social policy is also creates considerable problems. In general, the term “policy” can represent “a definite course or method of action selected from among alternatives and in light of given conditions to guide and determine present and future decisions” (Merriam-Webster's Online Dictionary). It is natural to assume that social policy deals with social goals and choices that have to be done. Usually social policy is associated with state provision of some basic welfare services (health, housing, social services, education, pensions, unemployment etc.) aimed at increasing social welfare, that is, the well-being of all members of the society. However, similarly to the concept of the welfare state, wider definition of social policy may encompass also some other services that develop the society's well-being (like transport, economic development, law and order, telecommunication etc.) and it may even include the general policy-making (that is economic policy) and regulation from the state aimed at improving living conditions. Mishra uses such broad definition in which social policy “refers, in a generic sense, to the aims and objectives of social action concerning needs as well as to the

structural patterns or arrangements through which needs are met” (Mishra, 1977: x).

Social policy is associated with satisfying some basic or higher needs, defined as the lack of something without which one cannot be either fully human, autonomous (the fundamental physiological and safety needs, as defined by Maslow) or a member of society (some higher-criterion needs like belonging and love, esteem, self-actualisation that can be achieved via providing social and political rights, right to work and to be a member of society).

There are several competing theories concerning the society and origins of social policy (for a detailed discussion see: Vic and Wilding, 1976). Functional theories, either sociological (order theories) or political (pluralist theories) emphasise social policy as an inevitable and naturally evolving tool for solving social conflicts, pursuing of common interest and avoiding conflict harmful for the society (see Vic and Wilding, 1976: 3-6). Therefore social policy is a product of social and economic changes, not a product of intellect or reformers. However, the weakness of such approach is that social policy is perceived as “inevitable” or “functionally necessary” and that there is a causational assumption about its “neutral” or “generally beneficial” consequences (Vic and Wilding, 1976: 7-8). Theories of conflict (sociological) and elitist (political) both underline that the conflict is a central issue in society being a natural product of achieving consensus between different social or political groups in society. Thus, social policy is “primarily the result of the constant attempts of various groups in society to improve or redefine their situation vis-à-vis these other groups.” (Vic and Wilding, 1976: 18).

Although existing from early times, social policy as a science emerged from economics in XIX century. Modern social policy<sup>1</sup> started to develop during industrial revolution in England and Germany as a new social class of workers emerged. As a science, social policy investigates sources and social costs of economic growth. It “(...) explores the social, political, ideological and institutional contexts within which welfare is produced, distributed and consumed” (Erskine (1997: 19).

The main aims of social policy include providing every member of the society with equal rights, minimum standards and opportunities and protection against social contingencies. Although these purposes already do assume some redistribution, a state can also declare an intention, as a part of her social policy, to

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<sup>1</sup> Historical development of social policy in the UK and USA is presented by Barr (1998) in chapter 2. Other positions related to history of the welfare state: Ashford (1986), Flora (1985-86), Flora and Heidenheimer (1981).

smooth income and welfare inequalities. Esping-Andersen postulates that social policy should “emancipate workers from market-dependence” and to “minimize the importance of market-generated income” (Esping-Andersen, 1990: 26), therefore weakening the advantage an employer has over an employee.

De Neubourg and Weigand (2000) propose a definition of social policy as “the social management of risks” (De Neubourg and Weigand, 2000: 17) and discuss its active role. Such policy should not limit itself only to the ex-post measures (state interventions motivated by efficiency and equity grounds), but should also apply some prevention course. They emphasise that, particularly in modern economies, social policy should not operate only with the direct management of risks, by providing goods and services that would satisfy social needs, but rather it should focus on providing the *means* to get access to the fulfilment of these needs. In other words, social policy should enable individuals a full and free access to housing and utilities, to food, to health and sexual reproduction, to social participation and “*the basic mechanism* (italics in original) that guarantee the fulfilment of these needs”, that is an access to income. In the case of modern developed economies, there are two focal areas, to which such an entry should be granted: labour market (“as the main income-generating mechanism”) and education (“as the main source for future income”) (De Neubourg and Weigand, 2000: 9).

The main areas of social policy include labour, retirement, housing, health, educational, demographic, family, cultural, environmental and immigration issues. Usually, provision of security, both in terms of physical protection and human rights “is not defined as a part of social policy” (De Neubourg and Weigand, 2000: 9).

### **Ideological foundations of social security**

The shape of the welfare state and its social policy is definitely determined by subjective perception of values. Nicholas Barr presents an interesting two-stage approach to analysing social policies (Barr, 1993: 4). According to him, social policy deals with two types of questions. The first question concentrates on social policy aims and has normative or ideological (subjective) character, while the second question is about the methods of this policy and represents purely technical (objective) element. The first stage of policy making is moved by economic interests (class or group “rent seeking”) and moral values (“a social value lag”, Vic and Wilding, 1976: 20).

Relating to the second stage, one might question the pure objectivity of method choices. In real terms, even this phase is strongly influenced by political and

socio-economic factors shaping, or at least quite strongly defining the range of, possible solutions (an example is political economy of pension reforms).

The social policy of the state aimed at providing welfare involves the state's intervention in economy which is achieved by fundamental tools of taxation and legislation. They usually implicate reduction of personal property and freedom; thus an ideology is needed to justify this action upon some set of commonly shared values. However, such values have unavoidably political character.

Several mainstream ideologies propose different role of state and extent to which state should intervene in the economy (for detailed discussion of these issues see Barr, 1998: 44-64, also Vic and Wilding, 1976). Those ideologies have a direct impact on how the issues of private property, taxation, redistribution, regulation and public production are perceived. Knowledge of underlying doctrine helps also in assessing some particular solutions and reforms (for instance, pension systems).

Libertarians (represented by natural-right libertarians like Nozick and empirical libertarians like Hayek and Friedman) propose that state should perform only fundamental safety function (produce certain public goods) and should not intervene in the market as it might reduce the total welfare of the society. They motivate it also on moral grounds as any of state activities infringe individual rights for freedom. Substantial state intervention is socially disruptive, wasteful in resources, promotes economic inefficiency and obliterates individual freedom (Barr, 1998: 47).

Utilitarians (like Beveridge, Keynes and Galbraith), on the other hand, assume that even though the capitalistic system is the most efficient one, it also creates some costs (poverty, inequality) that can and should be ameliorated by state (Barr, 1998: 48). Therefore, there exist some areas where public policy can improve social welfare (although not all of those actions are Pareto-efficient). Moral justification for state's involvement is given in Rawls' theory of justice.

Democratic socialists support the welfare state and either see it in terms of common consensus, or treat it as a useful but transitory stage to creating socialism. Radicals, like Marx, argued that the welfare state is an instrument of capitalistic oppression (class conflict theory). Marxists accuse social policy of emphasising technical, administrative attempts to solve what are essentially political issues. (Vic and Wilding, 1976: 13). Some more moderate socialists see the welfare state as a tool acting in the interest of ruling class (elitist theory) but also – to some extent – the workers themselves (Barr, 1998: 63).

**Table 1 Basic ideologies and their values.**

Ideology		Values
Libertarians	natural-right libertarians empirical libertarians	individual liberty, ethics
Liberals	utilitarians Rawl's theory of justice	utility maximization justice
Socialists	democratic socialists marxists	equality, freedom, rights and needs fraternity, needs

Source: Based on Barr (1998: chapter 2).

Shionoya (1998) argues that the current crisis in the welfare state is caused not only by economic and demographic factors and that it should be analysed also in the context of ideological background. In modern countries, not only free-market but also a market for medical services or pension system do play important social and economic roles. Therefore, the welfare state as a whole (that is social policy and its institutions, mainly social security) “must depend on certain moral values that articulate and justify the body of policies, rule and practices of social security” (Shionoya, 1998: 1). He reasons that one must know these principles to be able to control legitimately the welfare state. Since the moral values are of very subjective matter, it is natural that people should work out compromise and base the welfare system on commonly shared principles that emerge in the process of social agreement. Without those moral principles it is easy to succumb. The author states further, that “[m]oral principles rather than mere fiscal considerations are needed to restructure the welfare state in the developed countries” (Shionoya, 1998:1). Of course a unanimous agreement is impossible as “[n]o society can accept all forms of value systems and behaviour. Social problems of this type are part and parcel of life in society” (Vic and Wilding, 1976: 18).

### **Types of social policy and their role in modern society**

Based on the ideologies presented above, scholars have worked out various typologies for existing welfare states. Though such delimitation naturally concerns clear cut-off “ideal” types, it helps to understand particularities of each country social protection, for instance pension systems, and gives some ideas with regard to possible reforms.

One of the most popular typologies is a three-model created by Titmuss (1974) who distinguishes between three types: residual model (public assistance model), motivational or merit-oriented model and institutional model (c.f. Rymsza, 1998:

29-31). In the first type, market and family are the main providers of social needs; social assistance is available only as a temporary measure in case the first two sources fail. The second model is achievement-driven and its social policy is treated as an additional, assistant element to economic policy. Within this framework, help from the state is conditioned on individual performance, which strongly supports any kind of insurance with actuarial equivalence between payments and benefits. The last model is based on strong public redistribution. Social policy here is an integral tool for achieving social cohesion, with redistribution taxes and programmes aimed at income equalisation. The social goods and services are provided on the basis of needs.

In his seminal study of modern welfare states, Esping-Andersen (1990) proposed three types of “regimes”, being particular constellations of social, political and economic arrangements, constituting specific types of social policy (cf. Rymsza, 1998: 29-31, Herman, 2003: 8-9). Social protection is measured by its degree of “de-commodification” (Ebbinghaus, 1998: 7) which “occurs when a service is rendered as a matter of right and when a person can maintain a livelihood without reliance on the market” (Esping-Andersen, 1990). Also, “[...] Esping-Andersen stresses the redistribution function of social policy, in particular, whether universal citizenship rights correct market inequalities” (Ebbinghaus, 1998: 7).

The first model prefers selective social-assistance programs with strict targeting at lowest income individuals. The liberal political tradition implies that the state’s involvement should be limited to a minimum so as not to create negative labour incentives and limit individual choice. The social right to receive public help is based on the notion of citizenship; however a beneficent must pass the mean test and often suffers from stigmatization. Close to this model are the Anglo-Saxon countries (see Table 2).

The conservative model is based on paternalistic state conservatism, Catholic tradition and corporatism that attribute rights to social services and goods on the basis of contributions. The main tool of social policy is the mandatory system of occupational private insurance backed by the state’s social insurance. Such a system reveals tendencies for keeping the social status quo. Originating from Germany, the conservative model spread over the Europe and became to be known as the “continental” model. With regard to it, Ebbinghaus (1998: 9) proposes a separate class (“Latin particularistic-clientelist subsidiarism”) for continental Latin welfare states of France, Italy, Spain and Portugal arguing that – in contrast to Germany – these countries introduced compulsory social insurance much later.

The third type of welfare state regimes, the social-democratic model is based on the ideology of socialism and strives for equal society and social safety however historically it is an extension of notion of T. H. Marshall's (1950) social citizenship (Rymsza, 1998: 35). The universal level of benefits according to social-democrats should be much higher than the liberal basic needs (Esping-Andersen, 1990: 7). This model best describes the Scandinavian countries.

Marshall's (1950) concept of social citizenship consists of three forms: civil, political and social rights. Lemke (2001) observes that each of them developed gradually, first civil rights (for instance: freedom of speech, religion, the integrity of body) being a product of the 18<sup>th</sup> century French and American revolutions, next political rights (voting rights, citizenship, political participation, political representation) that developed at the end of the 19<sup>th</sup> century and finally, social rights (basic support and income or rights to welfare) emerging in the second half of the 20<sup>th</sup> century (Lemke, 2001: 7). Another classification of rights (Birchall, 2003) distinguishes between claim rights (implying duties on other people, for instance for social security benefits), liberties (like free speech, personal freedom, freedom of religion), powers (ability to perform some actions, examples are driving licence, parent rights, ownership rights) and immunities (exempt from some duties, legal obligations, laws etc.).

**Table 2 Welfare state regimes and social policy implications: Esping-Andersen model.**

Type of welfare Regime	Liberal	Conservative/Corporatist	Social Democratic
<b>Values</b>	Work ethic stigma	Rights according to class and status	Equality, universalism of high standards
<b>Aims</b>	Strengthen market	Strengthen civil society, limit market	Fusion welfare and work, full employment
<b>Social rights</b>	Citizenship	Employment-related	Universal
<b>Welfare provision</b>	Mixed services	Transfer payments	Public services
<b>Benefits</b>	Flat benefits	Contribution-related	Redistribution
<b>Instruments</b>	Means tested assistance	Private insurance backed by state	State = first line of support; high level of benefits
<b>Decommodification</b>	Low	Medium	High
<b>Class implications</b>	Middle class suspicious of state	Class maintained but stabilised	Middle class wooed from market to state
<b>Country example</b>	USA, Canada, Australia, UK	Austria, France, Germany, Italy	Scandinavian countries

Source: Herman (2003) and Ebbinghaus (1998).

In light of the above discussion it is interesting to ask how developed countries in Asia, particularly Japan should be categorised. It seems to me that, although Japan's low public spending on social security might indicate the liberal model strong occupational relations speak in favour of the conservative model. To some extent, Japan features Titmuss' residual model in the public segment in connection with official public programmes, while it is conservative with reference to the private occupational sector. The difference is that in the Japanese context, the basic institutions providing social support are family and company. Such a description quite clearly reflects a construction of Japanese pension system (modest public flat component and quite generous occupational part). However, the current status of family has been undermined by demographic, sociological and economic changes (increasing unemployment and lingering perspectives for the life time employment). Economic difficulties affect the position of company. All those factors increase uncertainty and are likely to change the current system. Also, current social security structure will perhaps have to switch from pension-oriented to more healthcare-oriented one.

Personally, I would be inclined to support the welfare state understood as a composition of a) pragmatic expenses derived from the state's natural function of preserving law and order and b) ideology-based expenses aimed at providing some minimum level of safety for the state citizens as a natural result of social contract. In my view, citizens should, in return to their tax payments and other services granted to the state, be given some equivalent right to safety in the case of personal misfortune. Therefore, my perception of the right to the welfare is derived from the mutual rights and obligations binding all the members of the society (social contract) and perhaps locates somewhere between, but closer to, conservative and socio-democratic models.

Some more technical typology of social policies can be created on the basis of particular solutions. The welfare state can be mandatory vs. discretionary, can offer selective benefits and services (available after passing some requirements, for instance means test) or universal ones (available to all those who need them). Also, there may exist some quasi-contractual or mutual benefits that are universal but only after having earned these rights. Social insurance is such a case. Of course each solution has its pros and cons. For instance, a universal model creates social solidarity, promotes altruism and is easy to administer, however is expensive and also there are some problems with proper targeting the potential beneficiaries. More

selective programmes are cost efficient, perhaps more difficult to administer (targeting issue), potentially stigmatising and therefore, creating low take-up problems. Constructions based on mutual contracts offer some positive features, however is hard to apply in societies with strong income inequalities.

## **2. Social security as an element of modern state and a domain of social policy**

Social security represents an essential part of the welfare state: “The social security delivers a key element of the complex and highly regulated network of conditional support provided by the state to citizens who lack the financial or physical means to meet their basic needs.” (Harris, 2000: 4–5). Social security is also a domain of social policy which, together with economic policy and more recently environmental policy, contributes to a somehow more general concept of well-being. However, what exactly is social security?

### **Discussion on the definition of social security**

As many other social-related concepts, this one is neither clearly defined. Any attempt must probably end as a functional definition rather than an objective one. Each country has its own system that is based on its nationality, values, socio-economic situation, tradition, politics and etc and as this background varies between countries, so the mechanisms and rules for social security. Each ideology shapes roles and functions of social security being probably one of the most important sources for the divergence of definitions. With regard to the applicability of the same social security solutions in different countries, the general conclusion is that, “[a]s long as societies differ in their cultures and value, it is unlikely that social welfare provisions in any two countries will be the same, either in form or in spirit” (Chow, 1987: 39 quoted in Sanders, 1997: 3).

There is neither universal object that may serve as a designate, nor a definition in the international law (cf. Pieters, 2000:1). However, there is some intuitive knowledge about the social insurance and this, I suppose, probably evolves from some common need of protection and generally shared views and fundamental values.

The English expression “social security” appeared for first time in the Social Security Act of the United States, enacted in 1935. However, at that time, some European countries were already run social insurance programmes as an element of their social security systems. Social security at the time of its implementation was understood in USA as “a system of guarantees to individuals against loss from

major and minor catastrophes arising from social, political, and economic institutions and practices” (Gagliardo, 1949: 10). Its functions reflected (and still do) the liberal ideology of minimalist involvement of the state:

“One important difference is that social security systems are designed to provide incomes that will maintain a minimum standard of living when earnings are interrupted rather than to supplement regular earnings or to make up the entire loss, or nearly the entire loss, suffered. (Gagliardo, 1949: 15).

and as quite picturesquely described by Edwin E. White - a scholar of those times cited in Gagliardo (1949), to those who believed in social insurance (c.f. further points discussing the differences in terminology between USA and Europe), as the main mechanism of the system:

“[...] social security means not a feather bed, provided at public expense, but a net to catch those who fall, or rather, a floor which will assure all Americans in all contingencies of life a minimum of income sufficient for an existence in accordance with prevailing concepts of decency. Anything above such a minimum, the citizens individually must still provide for themselves through private insurance and other savings” (Gagliardo, 1949: xviii-xix, introduction).

In 1950 the Japanese Advisory Council on Social Security described social security systems as “(...) the systems to enable every citizen to lead a worthy life as a member of cultured society” with provision of “countermeasures against the causes for needy circumstances including illness, injury, childbirth, disablement, death, old age, unemployment and having a lot of children by implementing economic security measures through insurance or by direct public spending” (MHLW, 1999: section 2). This definition, therefore, underlines the techniques and programmes (plural form “systems”) and presents a detailed list of typical social risks (cf. point 3.).

One of the most important documents is 102 Convention (ILO, 1951) of the International Labour Office ratified by 40 countries (as of November 2003) which specifies minimal norms in social security. The ILO definition is based on instruments and it understands social security as a response to the people’s need for the widest security (Pieters 2000: 2) rather than as a set of various mechanisms that serve achieving this security. It provides a minimum income (safety-net) as a direct financial assistance to specific groups unable to earn income adequate for their needs (Saunders, 1997: 4).

A short and concise non-instrumental definition, that is the one enumerating some situations for which the state provides or should provide protection against

human damage, is presented by Pieters (2000: 2) who describes social security as “the body of arrangements shaping the solidarity with people facing (the threat of) a lack of earnings (i.e. income from paid labour) or particular costs). Some other definitions focus on such functions as risk protection, lifecycle smoothing, income redistribution and mutual assistance based on social solidarity:

“Social Security in developed countries typically combines three different elements: income tested social assistance designed to relative poverty, social insurance concerned with the provision of security and the spreading of income over the lifecycle, and categorical transfers directed at redistribution between specific groups” (Atkinson, 1989: 16).

Atkinson (1989: 99) attributes dual meanings to social security, as an objective of government policy and as a set of policies, while Titmuss stresses the functional aspect and defines social services produced by social security “based on common aims, rather than the mechanisms designed to achieve them” (Harris, 2000: 15). Similar definition of social security is provided by Saunders (1997). In his view,

“[s]ocial security refers to the design and implementation or encouragement of activities intended to meet the basic needs of vulnerable individual and groups in society by guaranteeing their physical survival and by protecting them against unforeseen risks against which they are unable to protect themselves” (Saunders, 1997: 2-3).

According to this definitions, three basic ideas should be emphasised: possibility to identify needs relatively easily; possibility to identify cases where those needs are not met, either with regards to the needs themselves or the social classes; and in the end possibility to “design, legislate, implement and deliver (or otherwise encourage) social security arrangements to meet those needs” (Saunders, 1997: 3). Saunders emphasises that “(...) *social security is an end rather than a means*” (Saunders, 1997: 3, italics in original), that is, that it should be based on particular goals and needs rather on particular strategies or techniques.

With regard to the organisational structure, social security may include: social insurance<sup>2</sup> only (USA equivalent, see further discussion about the terminology differences), social insurance and social assistance (definition in the UK) or social insurance, social assistance and health protection (Rymsza, 1998: 7). This wide definition is applied also in Poland. Singular form (“ubezpieczenie społeczne” which reads as “social insurance”) underlines a particular technique or institution of social security while plural form (“ubezpieczenia społeczne” – “social insurances”) refers to a whole system, comprising of various programmes (Rymsza, 1998: 20).

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<sup>2</sup> It is characteristic that the word “social insurance” is a title of Gagliardo’s (1949) book describing American social security system.

The term “social security” in the European Union encompasses the social solidarity concept and “reflects a common social and economic commitment towards its recipients, particularly the unemployed” (Harris, 2000: 15) based on the already discussed social citizenship. This social solidarity provides a legitimization for a redistribution system operating either horizontally (intergenerational redistribution/solidarity) or vertically (income redistribution/citizenship solidarity). It also corroborates the idea of insurance equivalence meant as risk sharing between the insured, and not the strict actuarial equivalence between contribution and benefit (cf. Rymsza, 1998: 20-21).

Very closely related is the term of “social protection” understood as “public measures to provide income security to the population” (Holzmann et al., 2003: 5). In many cases their meanings are simply the same. However social security may be characterised as a comprehensive mechanism typical to developed countries but “less applicable to new areas such as community, micro and area-based schemes” (Ortiz, 2001: 657). In its report on social protection in Asia and Pacific, scholars from The Asian Development Bank classify social protection as

“the set of policies and programs designed to reduce poverty and vulnerability by promoting efficient labor markets, diminishing people’s exposure to risks, and enhancing their capacity to protect themselves against hazards and interruption/loss of income. The policies and procedures included in social protection involve five major kinds of activities: labor market policies and programs, social insurance programs, social assistance, micro and area-based schemes, and child protection (Ortiz, 2001: 657).

Therefore, social protection can be seen as an extension of the modern social security (environmental policy, new approach to labour markets, programmes fighting with social exclusion and negative demographic effects etc.), particularly in developing countries that have to deal with traditional set of problems but also some issues characteristic for their economic and socio-demographic situation (environmentally-safe growth, child protection, local and civic initiatives, micro-loans, education, anti-discrimination issues etc.).

### **Why social security emerged?**

Historically, social security as an institution had functioned in Western countries much before a common, yet indefinable name for it appeared. Initially, the basic sources for protection in local societies were family and local groups. However, the Industrial Revolution caused mass migration to the urban areas and changed the socio-economic conditions. Transport difficulties greatly weakened the workers’

links with the extended families in the rural areas, while some new types of risks (industrial accidents, sickness and disabilities as occupational income interruptions, old-age protection for salaried groups and diminished agriculture families). Consequently, it created a need for new system of protection that would be based more on the society as a whole rather than on the basic structure of society that is family and/or the local help.

The first social protection organised by state was introduced in Europe. In 1883 Bismarck established a first national health scheme with benefits from the state obtained on the basis of individualised, salaried work. The Economic Crisis of 1930s gave an incentive in the USA to create a national protection system, at least at the minimal level. Such safety net was introduced by the Social Security Act in 1935. New Zealand enacted its social security law in 1938 being proposed as a model by the International Labour Organization in its report of 1942 (MHLW, 1999: section 2). The United Kingdom introduced its social security system as a result of famous Beveridge Report of 1942. In comparison to the occupational-focused Bismarck approach (“earnings-related contributions giving entitlement to earnings-related benefits”), the Beveridge proposal concentrated on poverty relief as a main function of the system (Barr, 1998: 34). Social protection (shakaihoshō, “社会保障”, in Japan as an official concept appeared in its Constitution in Article 25 promulgated in 1946 (MHLW, 1999, sections 1 and 2). In the case of Poland, first social protection systems existed already before the First World War at the territories (partitions) occupied by Germany and Austria<sup>3</sup> and were developed on the basis of the Bismarck model after regaining independency (Rymsza 1998: 108).

### **Assumptions underlying social security concept**

Recent socio-economic developments create new challenges to social policy and call for re-evaluating its premises. During the post-war period, the developed states gradually stepped aside from the social security’s original framework of providing minimum conditions. Many new benefits originated and most of them are nowadays much above the minimum. In particular, the relative meaning of standard level of poverty, health and cultural requirements has changed, creating higher financial strains on the system.

Another issue is that, some forty of fifty years ago, the non-working periods in peoples’ lives (education, retirement and to some extent occasional brakes in

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<sup>3</sup> The history of social security in Poland is presented in Szubert (1987).

employment) were short in comparison to the working phase. However, nowadays societies require much longer time of schooling. Increasing life expectancy seriously amplifies the problem of support for the frail old population that is mainly in the pension provision and long-term care areas (cf. Bovenberg, 2002: 183-206 for pensions and MHLW, 1999: Vol. 1, Chapter 3, Section 1; Reinhardt (2002: 235-262) for health care); however there are also some less acute issues which relate to social inclusion. Since the length of non-occupational life period has increased there is a need for higher savings able to finance it. Current ways of financing seems not to be able to deal with this task anymore. All this issues need to be taken into consideration while proposing particular reforms.

The fundamental assumption underlying modern social security is the link between entitlement to benefits and an individual and paid labour. There have been several changes in the labour market and industrial relationships in the developed countries. People tend to have more diverse job careers; they do not work for only one-two companies during their lifetimes any longer. Also, some jobs do not represent classical employment contracts (outsourcing, part-time jobs).

A further serious problem is the assumption of full employment (Scherman, 1999; Shepherd, 2000). During the after-war growth period there were no great problems with unemployment. However, nowadays even the developed countries face relatively high unemployment. Shepherd (2000) states that the rising cost of social security is partly caused by “inequality of opportunity” and by “a huge and growing difference in incomes of rich and poor people”. Further, the author accuses the capitalistic industrialisation which creates negative socio-economic changes by promoting smaller families negatively influencing the family relationship, contributing to increasing speed of society ageing and leading to “people existing to the edges of society” (Shephard, 2000). In my opinion it is rather tricky task to answer what the causes of socio-demographic changes are and whether they are independent to the growth of economy or whether they depend on the formula of economy. Nevertheless, even though I do not agree with Shephard’s general line of casual reasoning (it is hard to argue that alternative economic systems would produce economic growth *and* avoid somehow natural changes in family structures, whatever negative they are; also it is a tricky question to link socio-demographic changes *only* to the formula of economy<sup>4</sup>), the outcomes certainly call for changes in social security design. Further, one can consent with the author’s remarks that

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<sup>4</sup> Such changes seem to be inevitably linked to the overall economic level of life and to the cultural changes, to which economic factors contribute only partially.

modern government, due to inclination for lowering costs of social welfare, are interested in promoting an informal welfare and that it is due to their liberal agendas that make them reluctant to pay for social security.

Discussing the family issues, one must observe that its structure has changed and that the reference model of the “classical” family (that is one consisting of working male, non-working wife and two-three children) used at the beginning of implementation of social security “is becoming less and less representative” (Scherman, 1999: point 3.3.3). Not only the working obligations distribution within male-female has changed, but also the employment prospects became tougher and less secure. Therefore, the mechanism under which the male is a bread-winner and a “gateway to various security measures” (Scherman, 1999: point. 3.3.3.) via derived rights must be revised.

The assumptions that lie behind the system are changing and social security is expanding its coverage and level of benefits which causes a natural evolution of the definition itself. However, the broader the definition, the more difficult it may be to distinguish this term from other techniques of social protection (Pieters 2000: 2). Scherman (1999) observes that “modern social institutions mainly developed during periods of almost continuously high levels of economic of growth” and therefore the societies used to make decisions that concerned shaping their social policies on the assumption of constantly increasing resources. Due to economics problems and demographic changes, this does not necessarily be the case in the future.

Consequently, especially in the context of developing countries, mechanical copying of “classic” rules underlying security system may not work. Even if all assumptions would be met, there may still exist disparate social risks. Pieters (2000: 2) argues that “(...) it has little sense to use the concept of social security for societies which did not (yet) introduce paid labour and/or where the work of the individual worker is only seen as a non identifiable part of the activity of the larger group”. He insists that it does not mean that such societies do not need any social protection. For instance, some modern African countries have different conditions (no regular or official work, no employment, more extended family structure, families living on benefits of one member etc.). In such countries, there is no much sense to rely on cash benefits, since the workers are not paid and the capitalistic economy is reduced to the barter (Pieters, 2000: 5). Kasente (1998) discusses a gender problem in Africa, where most woman work, but have no relation with social security as their work is not paid or is just part of the grey economy. Shepherd (2000) emphasises the problem of food and water supply which is another reason

why the ILO definition of social security is not applicable to most Third World countries.

### **Critique of the current social security framework**

All these facts lead to a somehow natural critique of social security in its current state. Pieters (2000: 5) claims that the social security is “passive” in this context that the social risks specified by traditional branches do not respond to the current problems and also that the assumptions underlying the social security concept must be changed<sup>5</sup>. Therefore, the European legislations (ILO’s definition) “do not serve anymore the purpose they were made for” (Pieters, 2000: 5) and the ILO definition is needed to be viewed from the current standpoint, “(...) which does not lead to the same conclusions as when it was first established” (Scherman, 1999: point 4.3).

### **Social security models in Europe**

One can distinguish two main types of social security regimes in Europe depending on whether there exists a strong relation between paid contributions and earned benefits (Conde-Ruis and Profeta, 2003). A system where such relation is strong there is low intra is called “Bismarckian”. The strong link implies that there are bigger differences in benefits and, due to proportionality between premiums and benefits, there is less intra-generational redistribution. Examples include Germany, Italy, France or Poland and are characterised by high replacement rates. The second type is called “Beveridgean” and features quite flat benefits with contributions proportional to earnings, therefore implying stronger redistribution within the same cohort. This category includes countries like the UK or the Netherlands (Conde-Ruis and Profeta, 2003: 4).

With regard to inter-generational redistribution one can speak of social security highly redistributing income (usually financed by the Pay-As-You-Go system) and of less redistribution nature (usually financed by fully-funded method).

### **Social security in the US and Europe**

As mentioned already, there are quite important differences in the scope of social security systems (cf. MHLW: 1999, Vol. 2, Part 1). The UK version represents the income security consisting of pensions and child allowances. Actually, similarly to the whole Anglo-Saxon liberal model, the equivalent name should be rather

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<sup>5</sup> Pieters discusses the assumptions of the standard family, but the issues discussed in the previous section are also of relevance.

“welfare state”. For instance, Nicholas Barr (1992, 1998) does not use the expression “social security” but rather terms such as “social policy” or “social services” which possess some wider range of meaning. In France social security covers social insurance (sickness insurance, old-age insurance) and old-age protection but does not include social assistance (cash benefits to the needy), social services or minimum income level security systems. All those elements together are labelled as “social protection” (MHLW, 1999: section 2). Germany, as mentioned, represents the continental concept with social insurance, social compensation and social support adding up to social security.

The biggest distinction exists between the European and American terminology. Americans use the expression “social security” to refer only to the retirement provision obtained under the OASDI programme (Old Age, Survivors and Disability Insurance, Martin 2000), while the term “social insurance” refers to social security. However, the U.S. Social Security Act includes some other programmes as well (unemployment insurance, health services, disability services, medical services for elderly and so on).

The very early tendency in US to use term “social insurance” in its social security context can be illustrated by a definition given by Dr. Rubinow in his work “Social Insurance” in 1915:

"Social insurance is the policy of organized society to furnish that protection to one part of the population which some other part may need less, or if needing, is able to purchase voluntarily through private insurance." (Rubinow (1934 : 508) quoted in Cohen, 1934).

Probably, due to its central point and little alternatives, social insurance was understood rather not as a tool of social security, but the concept itself being

“(…) a relatively inexpensive form of insurance, devised by the State to guarantee the wage earner and his dependents a minimum of income during periods when, through forces largely beyond his control, his earnings are impaired or cut off.” (definition by Abraham Espstein, quoted after Rubinstein (1934:508) in Cohen, 1934).

with typical security functions aimed at protecting

“(…) the worker and his family against the economic emergencies resulting from the temporary or permanent loss of a job through unemployment, sickness, invalidity and old age and against those other emergencies which arise from the death of the breadwinner, the illness and burial of a member of a family, the birth of a child or the burden of supporting a large family.” (ibidem).

The differences derive not only from purely terminological grounds. All documents and discussion concerning the Social Insurance Act of 1935 used the

expression “economic security”, so was the name of the committee [on social security] appointed in 1934 by President Roosevelt (Martin, 2000: footnote 9). However, “economic security” had narrower meaning (c.f. MHLW, 1999: section 2) and the initial intention of the legislators was to create a whole system of social security:

“Those who selected the title of the Social Security Act of 1935 had far greater aspirations for the phrase. It was chosen over its major rival, “economic security”, as the appropriate umbrella for a number of programs quite disparate in structure and focus: (1) federal grants-in-aid for three categories of state-administered public assistance—Old Age Assistance, Aid to the Blind, and Aid to Dependent Children; (2) a complicated tax-incentive scheme encouraging state-financed unemployment compensation programs combined with grants-in-aid for their administration; and (3) the totally federal Old Age Insurance Program.” (Martin, 2000).

Martin (2000) expresses an opinion that the main cause for the change of the perception of the “social security” phrase in USA must be attributed to the fact that each programme had to go through different agencies, congressional committees and, in effect, they were given legislation processes. Therefore, each part of the Social Security Act of 1935 “had such different political dynamics that they shortly developed independent direction” (Martin, 2000) and became unrecognisable for the public as a part of one common project.

### **Social security as a human right**

Social security is perceived as a human right which brings serious consequences<sup>6</sup>. Already in 1948 Article 22 of Universal Declaration of Human Rights stated that “Everyone, as a member of society, has the right to social security (...)” (quoted in Pieters, 2000, point 2). The Declaration states further, that this membership of society should give the person a right to participate in the organisation and resources of the State, and guarantee his or her economic, social and cultural rights that are essential for the person’s dignity and free personal life.

Furthermore, the UN Covenant on economic, social and cultural rights of 1966 once more acknowledges in its Article 9 the “right of everyone to social security and social insurance” (quoted in Pieters, 2000, point 2).

As pointed out, the international minimum standards of social security are set by the ILO Convention 102 which generally insists on providing replacement rate of

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<sup>6</sup> For instance reforming of pension fund systems aimed at limiting expenditures, can encounter strong opposition that uses human rights as a powerful legal background.

40% after 30 years of contributions (Fultz, 2002: 13, footnote 6, c.f. ILO, 1952). Many constitutions in the world recognise social security as a human or fundamental right (Pieters, 2000, point 2), for instance Japan in its Article 25 (MHLW, 1999: section 2).

At the European level standards were set higher by the Council of European Code of Social Security and its additional Protocol of 1964, with its later revised version (that is not in force due to lack of ratifications, Pieters 2000, point 2). Even though the welfare rights vary between countries, these social rights are “deeply embedded in all European countries” and included in the European Union law “in the “Charter of Fundamental Rights” adopted at the Nice summit in 2000” (Lemke, 2001: 7).

It should be mentioned that such an approach is fiercely attacked by liberals who claim that attaining unconditional and uncritical rights to the social services can result in excess demand for them, wasting resources (“free price”) and, in effect, in people’s dissatisfaction (Vic and Wilding, 1976). A situation where people, denied access to services, may feel robbed or deprived can lead to social disruption. A radical conservative writer, Enoch Powell claims that “translation of a want or need into a right is one of the most widespread and dangerous of modern heresies” (Powell, 1972: 12, quoted in Vic and Wilding, 1976: footnote 25). Such views, however, are hard to be put into practice, both on ideological and practical grounds. I would rather refer to it as some warning of possible distractions caused by too uncritical granting rights without necessary economic analysis.

### **3. Social security and social risk management**

In this paragraph I discuss shortly social risks, their characteristics and social security actions aimed at managing social risks.

#### **Definition and sources of social risk**

A risk can be understood quantitatively, as the possibility of occurrence of a certain event or qualitatively, as the event itself. Conventionally, as “risky” are labelled those outcomes that may bring negative consequences<sup>7</sup>. One should also distinguish between the concepts of risk and uncertainty; the former is of objective nature and “can be analysed mathematically” (Brown, 1999: 3) by assigning probabilities to the different possible outcomes; the later refers to those events

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<sup>7</sup> Although from a purely statistical point of view, a risk does need to be a negative result.

whose probability of occurrence cannot be assessed and thus, whose likelihood for occurrence has more subjective character. In the economic context, risk can be loosely identified as a situation when the future outcome of someone's activity (for instance value of investment, labour income etc.) negatively differs from the expected value.

Social risk can also be defined as an event *ex ante*, that is, as a prospect that the quality of life may decrease or *ex post* as a realized event, particularly in the context of salaried work; in this meaning any social risk refers to

“the lack of income from paid labour affecting those people who do not (or no longer have to) work due to old age, incapacity for work or unemployment; the passing away of one's wage-earning partner; the particular costs related to the upbringing of one's children; the need for (a coverage of the costs pertaining to) medical care; and the lack of the means necessary for a decent existence” (Pieters, 2000: 2).

Naturally, for most people in modern economies, salary work is the most popular of getting resources for living. However, we can extend this income maintenance context to all markets in general and also to non-market natural social groups offering support – that is family, friends and local societies. The definition in Neubourg and Weigand (2000: 11) is similar; however they do not mention social groups while describing social risks as “the risk not or no longer being able to rely on either markets or the family to secure the satisfaction of the main needs”.

Consequently, social risks are basically linked to the concept of economic security and I would consider social risks as possible events undermining security of an individual, both in the economic (narrow definition) and the welfare (wider definition) context. According to Rejda (1999: 2), economic security is “a state of mind or sense of well-being by which an individual is relatively certain that he or she can satisfy basic needs and wants, both present and future”. Thus, such a relative notion is very subjective and depends on the individual's perception, wealth, character, attitude, experience, social environment etc. Economic security consists of two layers: the first is the economic security as the ability of satisfying needs; the more general reflects some general stability of life-cycle incomes and living conditions.

Brown (1999: 4) stresses the actuarial underpinnings of economic insecurity as the inability to exactly predict future values of “variables such as rates of earnings, investment income, inflation, labor force participation (or unemployment), mortality and divorce”. He enumerates causes of economic insecurity related to: mortality, health status, job security (unemployment and changes in labour market),

inflation, retirement, divorce (financial independence) and dependants (upbringing, education). Recently, those sources of risks have been greatly increased by globalization of economies (c.f. Holzmann et al., 2003: 3).

Particularly pre-retirement actions are very complex and – due to the long horizon and rather unpleasant dimension of age and death – enhanced by consumer’s ignorance, thus creating a natural tendency for myopia and underestimation. It seems reasonable that the state should take up the task of designing and implementing (yet not necessarily managing) some social schemes dealing with old age and other social risks.

Social risks can be viewed in more material context (income insecurity, inability to satisfy basic needs), however, they may also be defined very widely, including social exclusion and psychological costs<sup>8</sup>. For instance, Zuckerman (1979) provides a psychological definition of social risk that I would associate with “higher”, not “material” needs; in such a context, a social risk is “[t]he estimated likelihood of being embarrassed, shamed or humiliated or of experiencing a loss of valued affection or respect of others”.

### **Typology of social risks**

Social risks can be classified according to various criteria. Holzmann and Jørgensen (1999: 9) propose three basic delimitations, that is, the depth, width and frequency of the loss. Catastrophic risks are those characterised by low probability yet huge potential damages; non-catastrophic risks have opposite characteristics. Depending on the range of affected households in a society, the risks can be labelled as “idiosyncratic” (or covariant risks), affecting individuals or single households, and “covariant” shocks hurting all wide groups or whole population. Finally, conditional on their occurrence, risks can be single or repeated.

Neubourg and Weigand (2000: 11-13) classify social risks according to the range of population to be affected by the risks. The first group consists of universal risks, shared by everybody (but not necessarily of the same probability), life-cycle risks (shared by some specific age or life-stage groups) and categorical risks (also called class- or group- risks) typical for certain socio-economic groups, for instance some profession or men-women. The second set includes incident, lifetime and

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<sup>8</sup> The notion of poverty is, particularly in developed countries, a relative concept. There may be a situation where individuals, even though being able to satisfy their basic needs suffer from social exclusion and to lead a “decent life”. Such exclusion can occur in the context of not being able to fulfill their cultural, spiritual or civic activities.

intergenerational risks.

A more comprehensive typology of Holzmann and Jørgensen (2000: 6, 12) is presented in their work on Social Risk Management.

**Table 3 Typology of social risks.**

	Micro (Idiosyncratic)	Meso	Macro (Covariate)
<i>Natural</i>		Rainfall Landslides Volcanic eruption	Earthquakes Floods Drought Strong winds
<i>Health</i>	Illness Injury Disability	Epidemic	
<i>Life-cycle</i>	Birth Old age Death		
<i>Social</i>	Crime Domestic violence	Terrorism Gangs	Civil strife War Social upheaval
<i>Economic</i>	Unemployment	Resettlement	Output collapse Balance of payments, financial or currency crisis
	Business failure	Harvest failure	Technology- or trade- induced terms of trade shocks
<i>Political</i>	Ethnic discrimination	Riots	Political default on social programs Coup d'état
<i>Environmental</i>		Pollution Deforestation Nuclear Disaster	

Source: Holzman and Jørgensen, 2000, Box 2: 12, adapted from Holzmann and Jørgensen, 1999, Sinha and Lipton 1999, WDR/Kanbur (2000).

### **Main branches of social security as responding to social risks**

As already mentioned, social security can be viewed as a one of three possible ways of managing social risks. While social security uses a set of public arrangements, the other two categories focus on informal activities or market-based solutions (Holzmann et al., 2003: 7-8). Naturally, such typology is quite sharp; for instance one can observe strong tendency for social security “privatization” taking place in recent years. By this term I mean here state’s attempts to use market mechanisms and private operators as main providers of publicly organised, supervised and often – guaranteed – system (vide the concept of individual retirement accounts and the Chilean pension system).

Both the ILO’s Convention 102 and the European Code of Social Security list nine branches of social security (c.f. Pieters, 2000: 3; c.f. ILO, 1952). Adding some

description of social risks one may arrive at the following list of social security benefits: old-age (risk of running out of resources after retirement), invalidity (injury, risk of accident and permanent inability to work) and industrial accidents, sickness (illness, risk of temporal or permanent inability to work) and medical care (risk of health expenditures, deteriorating health and diminishing working abilities), survivorship (risk that family members will have no resources to live after the death of breadwinner particularly important for the traditional family structure of two children and a non-working wife), maternity (risk of additional expenses and inability to work), family assistance (risk of additional expenses), unemployment assistance (risk of temporal or permanent inability to find work, plus additional expenses for searching for a new job).

Pieters claims that “this enumeration clearly reflects the structure of social security systems as they existed in the Western World after the Second World War” (Pieters, 2000: 4). Additionally, the legal structure of the minimum specified by the ILO or European documents is not suited to the modern reality. Those requirements are “tested only with respect to the standard beneficiary, which is still defined as a man with a non working wife and two children” (Pieters, 2000: 4). Consequently, Piers (2000: 4) suggest that the new social security approach should “take into account the broader diversity of family units” and be more concerned about the gender equality in the labour market.

### **Social risk management**

As already mentioned in section 1, de Neubourg and Weigand (2000) opt for more active social risk management. Such an approach should be aimed not only at meeting the needs caused by occurrence of risks, but also, or preferably, at making sure that individuals have a free access to the areas where they can fully fulfil their needs. (de Neuibourg and Weigand, 2000: 9-10). For instance, such a policy should enable households to cope with risks by providing them an opportunity to “sell” their labour at the market<sup>9</sup>.

The main reasons for taking up social risk management can be presented as follows (c.f. Holzman and Jorgensen, 1999: 7-8). First, it is poverty that not only deepens the vulnerability to risks but also can be regarded as one of their causes; therefore creating a vicious cycle. Second, managing risks brings about consumption smoothing for individuals and Pareto-improved welfare for society as it helps to

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<sup>9</sup> For instance, one typical response of households to increased financial pressures is initiation or increase of work by housewife's (see Horioka et al, 2002).

keep income stable and more predictable during all stages of individual's life-cycle and creates more stable environment for all members of society. The third reason focuses on improved income equity aimed at finding a balance between assuring equal opportunities and equal outcomes (elimination of drastic income differences). Be as it may, the ideological foundation of this premise (especially vertical income distribution) is somehow accepted in most of developed countries; however the level of preferable action is, obviously, different in various countries. The last reason can be described as an economic development-driven factor and sees social policy tools as an instrument that can contribute to economic stability and growth.

Holzman et al. (2003: 6-7) classify social risk management into three main strategies. The first group, prevention (or preventive) strategies, is used ex-ante and is meant to increase income and (or) reduce probability (variance) of occurring adverse risks. Preventive strategies include some elements of economic policy (for instance active labour policy, macroeconomic policy, environmental policy, human investments – education etc.). Social protection tools involve typically interventions aimed at improving labour market and skills level. The second group, risk mitigation actions, is based on ex-ante actions aimed at reducing the impact of future negative events. Usually such actions comprise of instrumental and temporal asset diversification and of risk pooling. Risk mitigation strategies may result in costs for the expected income (for instance insurance premium or alternative costs due to lower risk-return profile). Hedging can also be viewed as an insurance activity. Coping strategies are the third field of risk management. They are launched ex-post and are designed to relieve the impact of negative events. Coping can comprise of “individual dissaving, borrowing or relying on public or private transfers” in the form of charity or non-contribution programmes, i.e. means-tested transfers or public works (Holzman et al., 2003: 6-7, 8; c.f. also Holzmann Jørgensen (1999: 9).

#### **4. Aims, methods and techniques of social security**

##### **Functions of social security**

The role of social security is based usually on equity and efficiency grounds and - in more modern context – also acts as a tool of active social policy (social risk management) used to provide means to satisfy needs and to reduce dependency. Therefore, the main tasks of social security can be presented as follows (c.f. MHLW, 1999: Section 3). The first function boils to mitigation and coping functions,

therefore to dealing with the factors that can create situations of need (illness, injury, childbirth etc.) either through insurance techniques (social insurance) or by direct public spending (social assistance). The second issue is to ensure the minimum level of living by providing some kind of “safety net”; this function though still important, was most essential at the beginning of social security systems. The final role concentrates on economic and social stability and promoting economic growth. It is because, to some extent, social security, via its payments, can be seen as a shock absorber that helps to sustain aggregate demand during recession. More generally it is a tool for developing human capital and therefore it contributes in a long run to economic development.

The ILO’ functional definition of social security enumerates compensation of income loss, promotion of health and sickness prevention, creation of living conditions enabling realisation of common needs with particular support for elderly, handicapped and children (Scherman, 1999: point 4.3).

A common feature of social security is the need for income redistribution, both in the horizontal (between the rich and the poor) and vertical (between generations) context. To some extent, there exists also an inter-temporal redistribution for individuals themselves; saving for retirement is one of such examples. Redistribution can be achieved both via tax or social security systems. Nowadays there are various opinions in the perspective of old-age protection about whether the pension systems should perform the income redistribution tasks. While talking about traditional pension systems one is used to take their redistribution function for granted. However, there is no particular need for the “classical” PAYG old-age system to be redistributive in its nature. It can work without this, just performing the temporal transformation of resources that is the content of the intergenerational contract between the successive generations. The particular choice depends on social agreement; however it is also severely limited by pension system’s current economic situation.

### **Social insurance: a basic tool**

Social security can make use of several basic instruments. These are: “the family, voluntary arrangements of different kinds, private insurance, social assistance, mandatory saving plans, and social insurance” (Scherman, 1999: point 2.2). The way these, sometimes alternative to each other, components are put together in a particular country, is a political process. It is so because the degree and way the State intervenes influences the economic and social environments.

However insurance tends to one of the most convenient mechanisms of social management strategies aimed at risk-mitigation (cf. Holzmann and Jørgensen, 1999: 16, Table 1). Some informal or personal insurance actions cover for instance marriage, family or community arrangements. Formal (provided) solutions that can be mandatory provide insurance for unemployment, old-age, disability, survivorship, or sickness risks, belonging to the catalogue of social risks. At any rate, the mechanism of insurance has the distinctive features of collective social action aimed at immunization of risks thanks to common risk pooling.

There are several important motives for using social insurance by the state. The first group of the reasons is based upon the nature of the insured risks. Forss et al. (2000: 15) argue that “[s]ocial risks cannot be defined or calculated solely on the basis of individual risk”. Some of them, like for instance unemployment, inflation, congenial, chronic or any serious diseases (c.f. Barr, 1998: 125), cannot be properly handled with market or society-based solutions. Such risks may be too prohibitively expensive for an individual (if no risk pooling is provided or if arranging such a pool encounters problems due to group size, information costs and/or rational ignorance that all together prevent the Coarse theorem from working). The other possibility is that such risks may simply be uninsurable because of problems with estimation of probability<sup>10</sup> (c.f. Forss et al., 2000: 8) or/and due to catastrophic or universal (mass) character. In the later case even with a risk pooling the risks cannot be diversified away as they affect too huge part of population at the same time and may be linked up with overall economic situation (for instance unemployment).

The second group of the motives relates to the “information failures” (Barr, 1998: 124). Due to problems with asymmetric information such phenomena as adverse selection and moral hazard may occur (c.f. Forss et al, 2000: 8, Arrow, 1963: 961). Adverse selection is an ex ante problem which occurs when the insurer is unable to differentiate price/premiums according to risk levels due to lack of information. Thus, adverse selection involves a tendency for insuring lower-than-average quality risks, which results either in rising a probable threat of insurer’s insolvency or, if insurer tries to counterweight his lack of information by charging higher-than average premiums. Moral hazard can be described as a lack of incentives from the point of insured to behave prudently ex post (i.e. after concluding the contract), which results in increased loss occurrence that has to be met by insurer. These

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<sup>10</sup> In such a case, the “risk” is rather an “uncertainty” – see section 3 on social risks definition. In effect, “(...) social insurance, in sharp contrast with actuarial insurance, can cover not only *risk* but also *uncertainty* (Barr, 1998:126, italics in original).

information issues hinder the market mechanisms. If not provided any alternative, the society's well-being incurs a loss:

“The non-existence of markets for the bearing of some risks in the first instance reduce welfare for those who wish to transfer those risks to others for a certain price, as well as for those who would find it profitable to take on the risk at such prices” (Arrow, 1963: 946).

To some extent, social insurance is motivated by collective social policy goals (Forss et al., 2000: 16) and by collective consumption of public goods. Forss et al. argue that in fact “(...) any insurance contract can be interpreted as a process of public good provision” and emphasise that “[t]he key concept is collectivism, linking several agents to a shared value, in this case risk protection.” (Forss et al., 2000:13).

Because of the market failures and their inability to deal with uncertainties so many social institutions were created working with assumptions much different from the market-driven private insurance (cf. Arrow, 1963: 967). Comparing to private insurance, social insurance is characterised by quite loose actuarial relation (equivalence) between premiums and benefits and by compulsory participation (cf. Barr, 1998: 125) which makes this direct relation unnecessary (Swan, 1947: 345). Of course, the compulsion has several other functions such as avoiding myopic behaviour, free riding or eliminating information problems. Usually, it is difficult to assess the real cost of the schemes and the state acts as a monopolistic carrier of services (Gagliardo, 1949: 20).

Applied to retirement provision, social insurance programmes are typically government-run pay-as-you-go plans. Risk is shared even more broadly than in private defined benefit plans. The costs of adverse outcomes can be borne by the retiree (through reduced benefits), by current workers (through higher contributions), by the taxpayer (through tax-funded subsidies), and/or by future taxpayers (through subsidies financed by government borrowing) (Barr, 2002: 2; Barr 2000: 6). The premium-benefit in-equivalency results in income redistribution. However Forss et al. (2000: 9) notice that most redistribute income over the individual life cycle (especially in the case of pensions), rather than between households. Even such redistribution between individuals can be seen as a form of insurance in the long run (Arrow, 1963: 964). The reason is that when the premiums are paid based on the total group risk rather than subgroups or individuals, such redistribution guarantees in a long run an insurance against changes of personal characteristics.

### **Social insurance effectiveness**

Risk pooling, redistribution mechanism and large scale participation enhanced by compulsion give social security much higher capacity to deal with uncertainties. However, there are still necessary conditions to be met. In general, the risks must be “insurable”, that is, their probability must be lower than one and their occurrence pattern should be statistically independent. This is why insurance technique works pretty well when it comes to the old-age risk but does not show good efficacy in solving the problems of labour market during periods of economic decay affecting the whole working population.

### **Sources of financing social security**

In general, the sources of financing social security correspond to the methods that are used. The main sources include: insurance premiums, pay-as-you-go transfers (intergenerational contract), trust/programme funds and their gains from accumulation (investment gains, dividends and proceeds), surcharge on income tax or general taxes, mutual insurance funds and private insurance companies, borrowing and private charity. Each method of financing has its effect on the economy, capital markets, budgetary situations, labour decisions etc. In a wider context, the social security can be financed by reduction in benefits, namely, directly by beneficiaries.

Swan asserts that, due to taxing power of government, there is no need for separate and self-contained reserves (Swan, 1947:345), however also warns that the government “cannot practicably create a reserve in any form except its own obligations.” (Swan, 1947: 348).

The experience of social security expansion and politically motivated false “generosity” of the systems created serious financial imbalance and put strong strains on public resources. This explains current popularity of funded pension schemes, perceived to offer bigger transparency and an immunization from political risk. However, usage of general revenues can be only justified when a large part of the population is covered by a particular programme (c.f. Swan, 1947: 347). With regard to social insurance schemes, the author argues that since they offer benefits only to those who contributed, such framework can be financed either via pay-as-it-goes or there can be a reserve plan (Swan, 1947: 347). In my view, financing via insurance has the advantage of offering a transparent relation between premiums and benefits. It also provides some service at a specified “price”. Whatever the real price might be, it still limits the negative effects of “giving away”

for “free” the services; a typical free rider’s phenomenon in the systems’ where social services are provided at no or almost zero cost for a particular member. Naturally, those transfers must be paid back from the general resources and the final cost borne by the very individual might be, due to extensive over-usage, much higher than within a real price framework. Insurance mechanisms provide also incentives for risk-evasion and promote risk awareness and cautiousness in the society.

With regard to basic protection offered by the state Forss et al (2000: 6) emphasise that there exists widely supported belief that it “(...) should be financed by non-contributory arrangements, e.g. from general tax revenue” and that such solution would easily respond to the social need for basic protection and some general citizen rights guaranteed by law in many countries (cf. Forss et al., 2000: 6). They postulate self-financing and long-term financing as preferable methods to avoid “short-time political myopia” (cf. Forss et al., 2000: 17).

### **Future of social security in Europe**

The future of social security in the world will be definitely dictated by increasing need to create incentives for longer work and higher women’s participation in labour market; cutting state expenses and creating more self-made-man approach (vide concept of active social policy). The developing countries will have to attack the gender inequalities and create system not necessarily linked only to explicit labour contract.

Talking about Europe, Scherman (1999: point 3.4.9) emphasises the role of social solidarity and taking care of some particular types of families that are prone to fall into poverty. The scholar indicates also three problems present in European social policy, namely, the demography and need to keep the fiscal discipline of EMU, the more labour-oriented solutions for the Union and the enlargement process. In the area of pension protection, many authors call attention to the problems of unification of national rules and portability of accrued pension rights. Current pension solutions create a considerable obstacle to the increasingly mobile labour market; also there exist a strong problem with labour costs and the economic competition both in the international and internal European context.

Bearing in mind the problems above, it seems very likely that be tendency towards public “retrenchment” (see Weaver, 2003) will continue and that the role of the state in social security provision will be decreased.

It seems to me, that the welfare systems offered by the state will be further limited. Current trends (particularly in the field of pensions and health provision)

suggest more private schemes and higher role of stock markets. Such changes will be dictated by growing individualism, more sophisticated financial market but also by the need of developed countries to lower the costs of labour, especially in the less sophisticated industries. The globalisation offers therefore advantages, but can also trigger the run for downsizing the social facilities that have been achieved so far. The example of the US comprises a strong example for creation more competitive and less patrimonial economic systems.

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