Annex to Chapter 2: Social Protection

This annex describes the various organizational structures used by government units to provide social benefits and the effects of those structures on statistics compiled for the general government sector or the public sector.

A. Introduction

1. Many governments devote considerable economic resources to ***social protection schemes***, which consist of systematic interventions intended to relieve households and individuals of the burden of a defined set of social risks. ***Social risks*** are events or circumstances that may adversely affect the welfare of households either by imposing additional demands on their resources or by reducing their incomes. The relief is provided in the form of ***social benefits***, which may be payable in cash or in kind. This annex describes the different ways in which the provision of social benefits can be organized and the effect of each type of organization on the statistics of the general government sector and the public sector.[1]

B. The nature of social benefits

2. There is no universally accepted definition of the scope of social benefits, and the social risks covered are liable to vary from scheme to scheme and from government to government. The following list of typical social benefits illustrates their general nature:[2]

- Medical, dental, and other treatments and hospital, convalescent, and long-term care as a result of sickness, injuries, maternity needs, chronic invalidity, or old age. These social benefits are usually provided in kind directly or by reimbursing households or individuals.

- Support of spouses, children, elderly relatives, invalids, and other dependents. These social benefits are usually paid in cash in the form of regular dependents' or family allowances.

- Compensation for a reduction in income as a result of not being able to work, either full or part time. These social benefits are usually paid regularly in cash for the duration of the condition or for a maximum period. In some instances, a lump sum may be provided additionally or instead of the regular payment. Included in this category are retirement benefits, unemployment compensation, and income replacement because of sickness, injury, the birth of a child, or other forced reductions in work.

- Compensation for a reduction in income because of the death of the main income earner. These social benefits are usually paid in cash, often in the form of regular allowances.

- Housing benefits in cash and housing services, which may be provided free, at prices that are not economically significant, or by reimbursing expenditures made by households.

- Allowances to cover education expenses or, occasionally, education services in kind.

3. Social benefits can be provided in cash or in kind. If provided in kind, the goods or services can be produced by the unit providing the benefits, they can be purchased by the unit providing the benefits from a market producer, or the households can purchase the

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[1] A more complete discussion of the issues involved in the organization and treatment of social protection schemes is in The European Commission, *ESSPROS Manual 1996* (Luxembourg, 1996). ESSPROS stands for European System of Integrated Social Protection Statistics.

[2] This list is adapted from paragraph 8.56 of *1993 SNA*. The Classification of Functions of Government (see Chapter 6) has a category labeled social protection, but its scope differs from the benefits listed here, notably by excluding health care.

goods and services and be reimbursed. Protection also can be provided indirectly, such as through preferential tax allowances and wage subsidies. Benefits provided in this manner are not considered social benefits in this manual or in *1993 SNA*.

4. A social benefit is always a transfer payment and is always provided in a collective arrangement. A transfer payment means that the benefits are provided without the recipients being required to provide something of equivalent value in return. Thus, allowances provided as compensation of employees or loans provided by employers to employees are not social benefits. Transfers are defined in more detail in paragraph 3.8 of Chapter 3.

5. The collective requirement means that social protection schemes exclude individual insurance policies taken out on the private initiative of individuals or households solely in their own interest. Some social protection schemes may permit or require participants to take out policies in their own names. In order for an individual policy to be treated as part of a social protection scheme, the risks against which the insured are protected must be social risks as described in paragraph 2 and at least one of the following conditions must be satisfied:

- Participation in the scheme is obligatory, either by law or under the terms and conditions of employment.
- The scheme is a collective one operated for the benefit of a designated group of people and participation is restricted to members of that group.
- An employer makes an actual or imputed contribution to the scheme on behalf of an employee.

6. When individuals take out insurance policies in their own names, on their own initiative, and independently of their employers or government, the claims receivable are not treated as social benefits even if the policies are taken out against the same kinds of risks as listed in paragraph 2. Saving arrangements that maintain the integrity of the participants' contributions and are restricted to protecting against social risks are not social protection schemes, even if participation is compulsory, because no insurance is involved. Under such arrangements, the contributions of the participants and/or their employers are kept in a separate account and are withdrawable under specified circumstances such as retirement, unemployment, invalidity, and death. In particular, defined-contribution retirement schemes, as described in paragraph 21, are not social protection schemes.

C. Classification of social protection schemes

7. Social protection schemes can be classified in several ways. For example, schemes may be classified as (1) contributory versus noncontributory, (2) compulsory versus voluntary, or (3) that of an employer providing coverage for its employees versus that of a government providing coverage for the general population.

8. Contributory schemes require the payment of ***social contributions*** by the protected persons or by other parties on their behalf in order to secure entitlement to the benefits. These schemes are referred to as ***social insurance schemes***, and the benefits paid by them are ***social insurance benefits***. Schemes operated on an unfunded basis by employers without actual contributions by employees are considered contributory schemes because employers are imputed to pay, as compensation of employees, the amounts necessary to secure coverage against the specified social risks, and the employees are imputed to pay the same amounts to the employer as social contributions. With noncontributory schemes, the eligibility to receive social benefits is not conditional on the payment of contributions by the protected persons or by other parties on their behalf. There may, however, be other eligibility criteria, such as a means test. These schemes are referred to as ***social assistance schemes*** and the benefits paid by them are ***social assistance benefits***.

9. Participation in social protection schemes is either compulsory or voluntary. Compulsory schemes may be established by law and/or regulation or by agreement between employer and employees. In some cases, a scheme may be mixed, where some people are required to participate and others are allowed a choice.

10. The individuals or households eligible to receive social benefits are either a group of employees or a segment of the general population. All social assistance benefits are provided to the general population, although possibly limited by eligibility criteria. Social insurance schemes that are imposed, controlled, and financed by government units and that cover the entire community or large sections of it are referred to as

social security schemes and the benefits paid by such schemes are ***social security benefits***. Schemes in which employers provide social insurance benefits to their employees, former employees, or their beneficiaries are referred to as ***employer social insurance schemes***, and the benefits paid by such schemes are referred to as ***employer social benefits***.[3]

11. The classification of social benefits is based on the type of scheme supplying the benefits and not on the recipients. Thus any benefits received by government employees from social security and social assistance schemes are classified as social security and social assistance benefits even if the government employer has organized an employer social insurance scheme to provide other benefits to its employees. Indeed, employer social insurance schemes are often designed to cover only those risks not covered by social security and social assistance schemes.

D. The units involved in social protection schemes

12. As just described, social protection schemes can be organized as social assistance schemes, social security schemes, or employer social insurance schemes. The units involved in the organization and operation of schemes could be general government units, public corporations, or private corporations.

1. Social assistance schemes

13. All social assistance schemes are organized and operated by government units. The benefits are paid out of the unit's general resources according to the specified criteria. That is, no revenue is earmarked for social assistance schemes. The obligation to pay social assistance benefits is an expense in the period in which all eligibility requirements are fulfilled. Table 6.1 in Chapter 6 presents the GFS classification of expense, one category of which is social assistance benefits, which is further classified as benefits paid in cash or in kind. Some benefits may be payable over several accounting periods, such as disability payments, in which case a liability for the future payments has been incurred and the present value of those benefits should be recorded on the balance sheet as described in Chapter 7.

[3]Employer social insurance schemes are termed "private social insurance schemes" in *1993 SNA.*

2. Social security schemes

14. All social security schemes also are organized and operated only by government units. In many cases, however, entire institutional units are devoted to the operation of a social security scheme. Such units, referred to as ***social security funds***, are special types of government units. All social security funds must be identified to implement the alternative methods of constructing subsectors of the general government sector.

15. The existence of a social security fund depends on its organization, not on any characteristics of the scheme, such as types of benefits provided or sources of finance. For a social security fund to exist, it must be separately organized from the other activities of government units, hold its assets and liabilities separately, and engage in financial transactions on its own account.

16. The existence of social security funds, however, does not ensure that all social security schemes are operated by social security funds. It is quite possible that some social security schemes, especially at differing levels of government, are operated by government units that are not social security funds. That is, statistics for a social security subsector may not include all social security schemes. If a social security scheme is not a separate institutional unit, however, there may be separate accounts to manage the scheme's finances, which would permit certain comprehensive statistics on social security to be compiled.

17. The primary receipts of social security schemes are social contributions. As shown in Table 5.1 in Chapter 5, social security contributions are classified according to their source, which may be employees, employers on behalf of their employees, self-employed, or nonemployed participants. In addition, social security schemes may receive transfers from general government resources and they may earn property income from the investment of their assets. For determination of a fiscal burden measure (see Box 4.1 of Chapter 4), it would be necessary to classify social contributions as voluntary or compulsory.

18. Social security benefits are one category of total social benefits and are further classified in Table 6.1 as being payable in cash or in kind. Some social benefits, particularly retirement benefits, will be paid years after the corresponding social contributions have been received. Because social security benefits can be varied at will by the government as part of its overall economic policy, there is uncertainty about the eventual payment or level of payment of retirement benefits. As a result, no liabilities are associated with social security schemes in the GFS system and an expense is recorded only when payment of the benefits is required. Because of the high expectation that retirement benefits will be paid, however, a memorandum item equal to the present value of the benefits that have already been accrued should be estimated as described in paragraph 7.145 of Chapter 7.

3. Employer social insurance schemes

19. There are several types of employer social insurance schemes, each with a different impact on the statistics of the general government sector or the public sector. Social insurance schemes are either funded or unfunded. A social insurance scheme is funded if there are identified reserves or accounts assigned for the payment of benefits. There are three types of funded employer schemes: those operated by insurance enterprises, those operated as autonomous pension funds, and those operated as nonautonomous pension funds. Unfunded social insurance schemes are operated by the employer without assigning specific accounts or otherwise creating special reserves for the payment of benefits. Instead, the benefits are paid from the employer's general resources.

20. If a public-sector employer organizes an employer social insurance scheme but contracts with an insurance enterprise for its operation, then the general government unit or public corporation that is the employer will pay the required social contributions to the enterprise on behalf of its employees, and all other transactions of the social insurance scheme will be the responsibility of the insurance enterprise. If the insurance enterprise is a private corporation, then its transactions, such as the payment of benefits and administrative expenses, investment of assets, and incurrence and liquidation of retirement and other liabilities, will not affect the statistics of the general government sector or the public sector. If the insurance enterprise is a public corporation, then statistics of the public sector will be affected by the operations of the scheme, but not the statistics of the general government sector.

21. If a funded scheme is organized and operated by the employer, then the scheme may be structured as an autonomous or nonautonomous pension fund. A scheme that provides benefits other than for pensions and other retirement benefits is treated as an unfunded scheme because no reserves have to be established. In general, autonomous and nonautonomous pension funds may be organized as defined-benefit or defined-contribution schemes.[4] In a defined-benefit scheme, the level of retirement benefits promised by the employer to participating employees is guaranteed and usually is determined by a formula based on participants' length of service and salary. The liability of a defined-benefit scheme is the present value of the promised benefits. In a defined-contribution scheme, the level of contributions to the fund by the employer is guaranteed, but the benefits that will be paid depend on the assets of the fund. The liability of a defined-contribution scheme is the current market value of the fund's assets. It should be noted, however, that defined-contribution schemes are not social protection schemes because no insurance is involved.

22. A pension fund is autonomous if it is a separate institutional unit, which means it must have its own assets and liabilities and it must engage in financial transactions in the market on its own account. All autonomous pension funds organized and managed by government units are public financial corporations, which are members of the public sector but not the general government sector. Similar to schemes managed by a private insurance enterprise, a government unit's primary responsibility with respect to the scheme is to pay the social contributions on behalf of its employees. The assets of the pension fund and the present value of the liability to pay retirement benefits are assets and liabilities of the public sector. The receipt of social contributions by the pension fund is treated as the incurrence of a liability to pay future benefits by the public sector as described in Chapter 9. The property income earned from the investment of the pension fund's assets is revenue of the public sector (see Chapter 5), and the property expense of the liability for future retirement benefits is an expense (see Chapter 6). The payment of the retirement benefits is a reduction in liabilities of the public sector (Chapter 9).

23. A pension fund is nonautonomous if the employer has established segregated reserves, but the organization and operations of the scheme do not qualify as an institutional unit. All of the assets, liabilities, transactions, and other events of the pension fund are combined with the corresponding items of the employer operating the scheme, which may be a general government unit or a public corporation. The treatment

[4]Defined-contribution schemes are also referred to as money-purchase schemes.

of the assets, liabilities, transactions, and other events of the pension fund otherwise is the same as with an autonomous pension fund.

24. An employer social insurance scheme is unfunded when the employer pays social benefits to its employees, former employees, or their dependents out of its own resources without creating a special fund or segregated reserve for the purpose. An unfunded scheme can pay pensions and other retirement benefits that generate liabilities or it can pay other types of social benefits, such as health care. An unfunded scheme is similar to a nonautonomous pension fund except that many transactions and assets cannot be specifically identified as being related to the scheme. For example, the income earned on the investment of government financial assets cannot be separated into income of the social insurance scheme and other income. In particular, there may be no record of the employer paying social contributions because there are no specialized reserves to which funds can be transferred. To maintain consistency of treatment with funded schemes, transactions reflecting the employer's expense for the payment of social contributions should be imputed as described in paragraph 6.18 of Chapter 6.