

European Subsidiarity Versus American Social Federalism: Is Europe in Need of a Common Social Policy? ¹

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"De welvaartsstaat is nationaal en internationaal. Dit is een spanningsvolle tegenstelling, tevens een dynamisch proces én een roeping" (Herman Deleeck, 2003: 39-40).

Abstract

In this lecture, I raise two questions. The first concerns the likelihood that high levels of social redistribution will survive in an expanded Europe without borders. The second question is towards what kind of European social policy we should strive for in order that developed welfare state regimes could be maintained *and* exported to countries where social redistribution is currently weak. I shall use as a heuristic tool the historical genesis of the American and the European social models. This comparison suggests that European social subsidiarity has not hindered the post-war development of Europe's welfare states; quite the contrary in fact. Conversely, American social federalism would appear to have rather stood in the way of the realisation of social redistribution.

A reassuring, but somewhat premature, conclusion from this comparison could be that a European supranational system of redistribution is not required (in view of the considerable differences that exist, it would in any case be hard to attain). I shall argue, however, that conditions today cannot be compared to those prevailing during the development of post-war European and American welfare states. Under the present circumstances, it is safer to assume that a European social policy does indeed need to be outlined.

For the European welfare states, this poses a tough dilemma. While a 'Europeanisation' of social redistribution might seem inevitable at first glance, in reality it would appear not to be feasible. Moreover, the experience of the US certainly suggests that social federalism can hinder welfare states if the constituting parts of the federation differ too greatly. So what (if any) common European social policy should be pushed for? My recommendation would be to try, by means of the Open Method of Coordination or OMC, to arrive at binding agreements regarding minimum social standards.

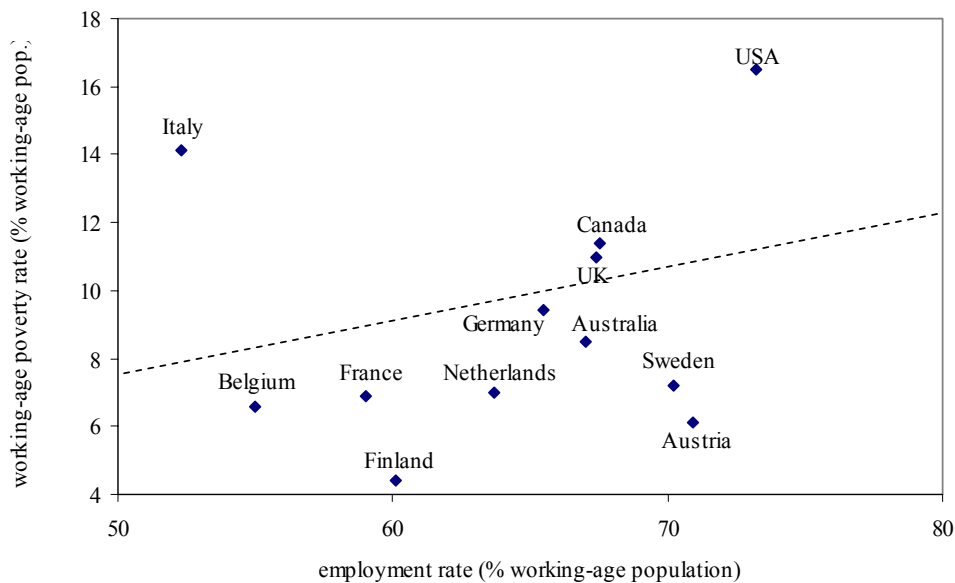
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1. Poverty, inequality and the Welfare State

Recent analysis of social protection politics point to one outstanding conclusion. If a country wants to achieve low levels of poverty it needs an important social redistribution and an adequate minimum protection for those in work and those out of work (Cantillon, Van den Bosch, 2002; Cantillon, Marx, Van den Bosch, 2003). While it has been clear for some time that social policy today must be aimed at reducing levels of benefit dependency by guiding more people to the labour market, adequate minimum wages and adequate minimum income protection in social security, remains of crucial importance to prevent poverty (Marx, 2004). This point can be illustrated by three simple cross-country correlations between employment, low wages, social expenditures and poverty.

Within any country, poverty among those with paid work is far lower than among those without work. However, between countries there is no such link between employment and poverty, as shown in figure 1, which plots poverty rates for the working-age population against employment rates for the late 90s. Actually the relationship is positive, implying that more employment is linked with more, not less poverty.

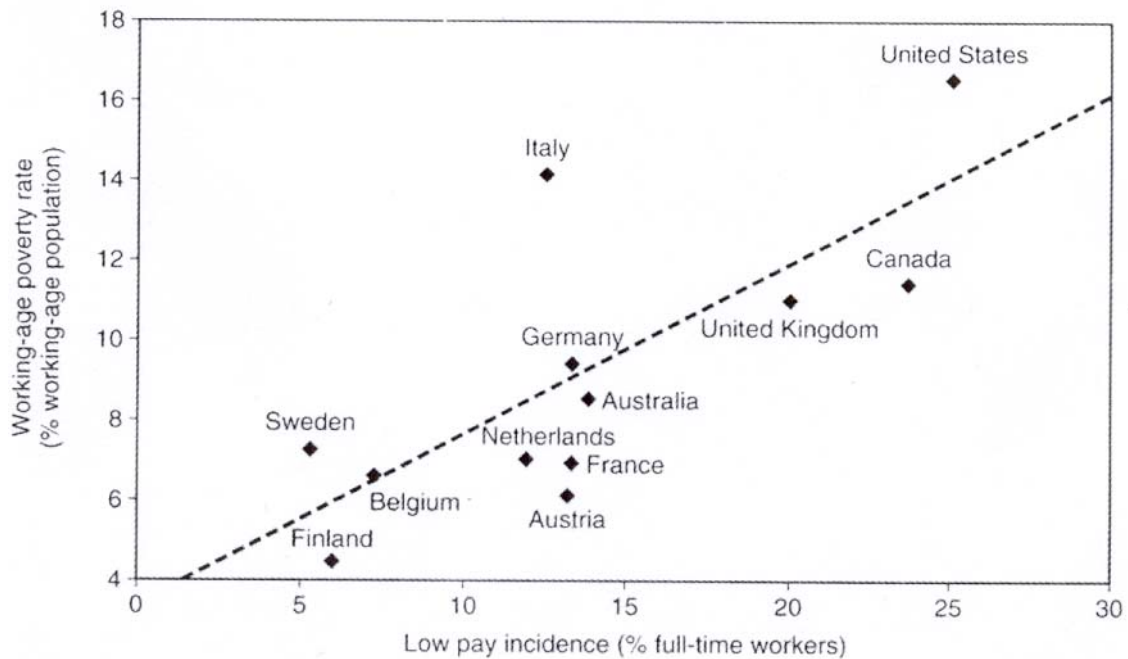
Figure 1. Employment performance and poverty.



Source: Cantillon, Marx and Van den Bosch, 2003.

The second cross-country correlation show there is a fairly strong relationship between the incidence of low pay and poverty among the working-age population. The seemingly obvious interpretation would be that a low-wage earner also tends to be in poverty. However this is only part of the explanation. The second explanation is that in countries where income protection for those in work is weak; the minimum protection for the non-employed too is weak. So, there seems to be a strong correlation between social protection of those in work and those out of work.

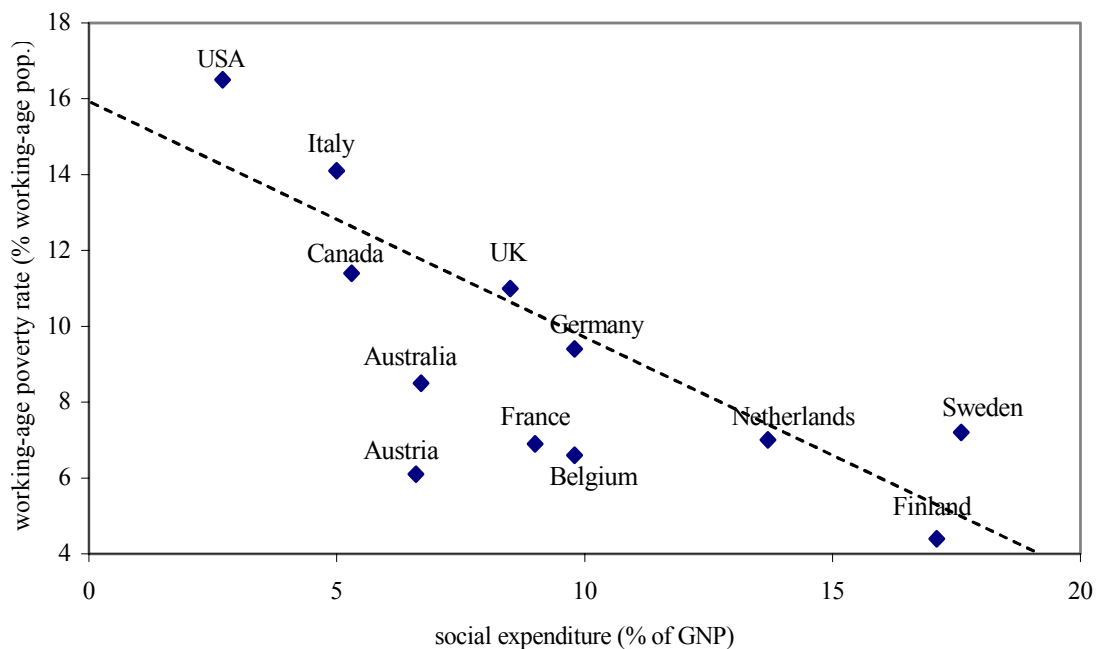
Figure 2. Incidence of low pay and poverty, mid-1990s



Source: Cantillon, Marx and Van den Bosch, 2003.

The third figure shows a negative relationship between social expenditure and poverty. This strong negative relationship has been well established: we refer to Cantillon et al., 1997; Bradbury and Jäntti, 2001; Atkinson, 2000; Beblo and Knaus, 2001; Oxley et al., 2001). It points to the importance of social redistribution for (income) poverty alleviation.

Figure 3. Poverty and Social Expenditures.



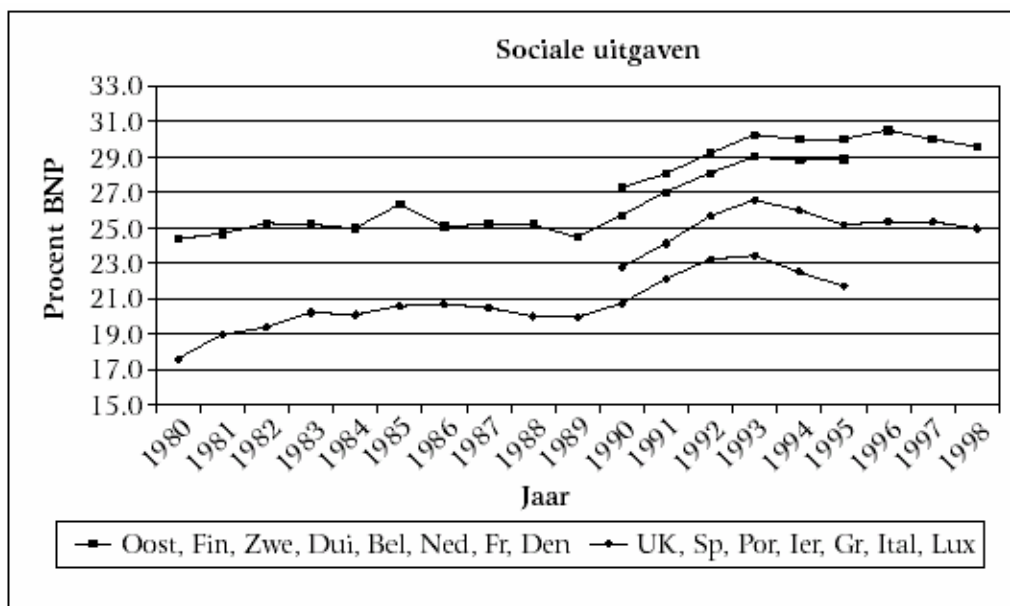
Source: Cantillon, Marx and Van den Bosch, 2003.

These empirical findings lead me to one important conclusion to start with: while it is clear that today welfare states need to reorient 'in order to become more active', social redistribution and an adequate minimum income protection in work and in social security remains of crucial importance to prevent poverty. The EU has an important role in this regard. The question however, is how the Union should play this role successfully.

2. How great is the danger of social dumping?

Economic theory predicts that, in a competitive world, developed welfare states must inevitably retrench their social policies. Consequently, small open economies (and small language communities) would no longer be able to sustain extensive social redistribution. Without a 'Europeanisation' of social policy (which, to understate it, is improbable) a 'race to the bottom' would be unavoidable. Numerous models have been put forward to give substance to this viewpoint². Moreover, this line of reasoning also seems to concur with many observers' intuitions.

However, until today, social expenditures do not point towards any form of social dumping. They indicate an upward convergence rather than a 'race to the bottom'³. The diagram below shows the evolution of social expenditures in high-spending countries (Austria, Ireland, Sweden, Germany, Belgium, the Netherlands, France and Denmark) and compares them with trends in countries where social spending is lower (UK, Spain, Portugal, Ireland, Greece, Italy). The first half of the 1990s was characterised by a convergence; in the second half of the decade, social spending in both groups of countries stagnated at a high level, at least in comparison to that in, say, the US⁴.



Source: Pestieau, 2002.

² For a survey of the literature, see for example Cremer and Pestieau, 2003; Wellich, 2000 and Cremer *et al.*, 1996.

³ Pestieau, P. (2003), *Are we observing a race-to-the-bottom? If not, why not?*, Université de Liège, CORE, Delta and CEPR, Prepared for the conference in memoriam of Professor H. Deleeck, September 18.

⁴ This conclusion is in line with that of Gali and Perotti. They find a clear overall trend fall in government investment as a share of GDP between 1978-1982 and 1988-1992 well before Maastricht (Gali and Perotti, 2003; see also Scharpf, 2002; Wilensky, 2002).

These observations constitute the basis for the generally accepted view that there are few signs of 'social dumping' and that – therefore – the argument shouldn't be taken seriously. This belief is, I think, unjustified for at least two reasons. Firstly, it is safe to assume that it takes some time before vested interests will yield to the effects of globalisation. Thus, it might simply be too early to draw any sound conclusions. Secondly, stagnating social budgets probably conceal declining social protection levels, as the number of beneficiaries is rising. Therefore, one should also consider trends in social benefit levels. The table below shows the development at micro-level of the most basic of social benefits, i.e. social assistance, as a proportion of average earnings. Although there is evidence of a sometimes worrying erosion of the level of welfare provided by such benefits in high-protection countries like Belgium, Norway, the Netherlands and Sweden, minimum benefit levels in some other countries actually rose or stagnated in comparison to wages. This was the case in Luxembourg, Austria, France, Portugal and Spain. Evidence is thus mixed. The welfare erosion of minimum benefits that has occurred in a number of countries can certainly not be regarded as an inevitable consequence of globalisation in the post-Maastricht era. After all, some member states with a high level of protection have succeeded in escaping the trend. However, the welfare decline of minimum benefits in others deserves closer attention and is, in any case, cause for vigilance.

Net social assistance as % of net disposable income at average wage level, single

	1992	2001
Austria	40	40
Belgium	38	35
France	24	24
Germany	25	24
Ireland	31	25
Luxembourg	47	48
Netherlands	49	37
Norway	26	23
Portugal	-	23
Spain	21	22
Sweden	46	38

- (1) Austria: Vienna; France: excl. housing benefits (incl. housing benefits 2001: 37%); Germany: average for all Länder; Norway: Oslo; Spain: Catalonia; Sweden: nationally guaranteed part of Cash Maintenance Assistance
- (2) Figures are derived from standardised calculations from national informants. They were asked to calculate incomes, taxes and child benefits for 4 model families (single, couple, couple with 2 children, lone parent with 2 children) at different earnings levels in their countries in 1992 and 2001. To check the validity of the calculations, comparisons were made with national and international data sources. We are grateful to Peter Abrahamson, Cecilie Wehner, Peter Krause, Gundi Knies, Tanja Zähle, Constanze Büning, Antoine Math, Theo Papadopoulos, Brian Nolan, Brenda Gannon, Yuri Kazepov, Geatano Proto, Stefania Sabatinelli, Monique Borsenberger, Wim van Oorschot, Michiel Luigjes, Axel West Pedersen, Anne Skevik, Charlotte Koren, M. Förster, M. Fuchs, Ana Cardoso, Joaquim Aiguabella, Raul Martínez, Adele Oliveri, Jonathan Bradshaw, Tina Davis, Kenneth Nelson for the calculations.

Source: Centre for Social Policy, Antwerp.

Given that the evidence is mixed, it is more prudent to take the 'fiscal-competition' argument seriously than simply to reject it. It is not because empirical evidence of a dramatic decline in social expenditures has not been found yet that this will continue to be the case in the future. The capacity of EU countries to manage redistribution within their national borders is probably declining: "Member states have lost more control over national welfare policies in the face of pressures from integrated markets than the EU de facto gained in transferred authority... The problem will be exacerbated by EU-enlargement" (Vandenbroucke, 2003). And while it is true that welfare states are a closed shop (De Swaan, 1994), in Europe the shop is open now. Moreover, mobility of workers, capital, services, care providers and patients is expected to increase in the future. Thus, we had better take into account that, without much closer cooperation in the social and fiscal fields, especially in the light of the imminent EU enlargement, the social model could come under strain from the dominant logic of economic integration. Jens Alber and Guy Standing formulated it as follows: "Our first conclusion is that there are no grounds for policy fatalism. This does not mean

that fears of social dumping are totally unjustified. On the contrary, unless governments and social scientists recognize that pressures in that direction – towards one variant or another of erosion – are present, they will fail to face the challenge by adapting their institutions, regulations and legislation to the new realities of the global open economy ..." (Alber and Standing, 2000: 116).

The question arises, then, what kind of European cooperation is required in order to safeguard developed welfare states while at the same time enhancing social protection in the less developed ones. In an attempt to try and answer this question, I shall employ as a heuristic tool a comparison between European subsidiarity and American social federalism in relation to the development of social redistribution in the post-war era. Admittedly this comparison is awkward, for several reasons. However, I deem it informative for the purpose of outlining the paths along which European social policy can and should develop in order to safeguard high levels of social redistribution.

3. The optimum level of redistribution: what does theory tell us?⁵

The European Communities, as a freshly established supra-national organisation, chose a fundamentally different path from the United States at crucial stages in the development of their respective social systems.

In the field of social policy, the United States reserved a sizeable role for the federal level of government, engendering a multi-tiered social architecture. This multi-tiered system actually combined federal social policy with a substantial competence for the individual states. The 1935 Social Security Act designated Old Age Insurance entirely to the federal level; Unemployment Insurance, Old Age Assistance, Supplemental Security Insurance and Aid to Dependent Children were all designed to operate under shared authority between the federal and the state level (Pierson, 1995; Weir, Orloff and Skocpol, 1988).

Contrary to the United States, the EEC chose in 1957 to leave the field of social policy to the national welfare states. This decision was taken on the basis of the Ohlin report, which had been commissioned by the ILO, and which concluded that social policy differences between countries were sustainable, so that harmonisation of national welfare states was not deemed necessary. The founding Member States made the strategic choice to focus exclusively on European economic integration, confident that the ensuing trade in an internal market would engender higher welfare for all, without any need to harmonise social corrections in the market at the European level. Thus, social policy was left to the discretion of the national welfare states, despite the fact that certain Member states did push for a greater European role in social policymaking.

Before we illustrate how both US fiscal federalism and European subsidiarity have developed over the years, we briefly consider the economic theory that influenced the political strategic choice of whether or not to federalise or, if you will, europeanise the domain of social policymaking.

⁵ Ninke Mussche and Stijn Baert were extremely helpful in the redaction of this chapter.

a) *Fiscal federalism*

Conventional economic wisdom suggests that redistribution within a federal system is best organised at the federal level. The basic argument for redistribution at the highest level originates in the observation that there are fundamental constraints on redistribution by lower level governments, namely labour and capital mobility resulting in a possible 'race to the bottom' (see among others Oates, 1972, 1999; Wildesin, 1991, 1994; Peterson, 1995).

The ability of individuals and firms to move freely from one jurisdiction to another is generally seen as a constraint on the amount of redistribution that each jurisdiction within a system of government can undertake. Local-level redistribution provides incentives for low-income families to immigrate and for high-income families -and indeed firms- to emigrate. An adverse selection problem may thus occur: individuals who expect to be net beneficiaries might be attracted to states/countries with generous social programmes, while net contributors might be deterred by the high tax burden in these countries. Consequently, the prevailing social protection systems could be confronted with increasing costs as well as a narrowing financial base, which would ultimately result in lower protection levels. Therefore, as was demonstrated by Oates (1972), a federal government should provide matching grants to help local government internalise the spillovers due to their public goods provision.

In *The Price of Federalism*, an influential book in the US, Peterson argues that delegating redistribution, besides welfare mobility, forces each state, or country, into a position in which they compete with each other to be the least attractive to people who need welfare. While local competition might be fine for most other purposes, it is disastrous for welfare policy. Each state, or country, will be racing to downgrade its welfare benefits to repel citizens who rely on public supports for survival. Another reason to start lowering protection levels might also be to attract high-skilled workers. A 'race-to-the-bottom' could be set in motion. Therefore Peterson (1995) summarises: "in a society where both people and business are highly mobile, it makes little sense to leave the marginal cost of welfare provision to lower tiers of government".

b) *Challenges to fiscal federalism*

The above model is rather intuitive but needs to be qualified in at least three respects, namely in relation to mobility, information and productivity. There are financial, cultural, institutional and political barriers to mobility. These barriers are obviously particularly high in Europe. Moreover, potential migrants do not have a perfect knowledge of and insight into the net benefits they receive in their home country, let alone those they might claim in a given host country. Thirdly, competitiveness is not only affected by labour costs, but also by such factors as productivity, infrastructure and social capital. Therefore, a high-tax country may nevertheless be a good place to invest if the nation uses the tax revenue efficiently to provide infrastructure and other services that would be more or even prohibitively expensive if one were required to provide them for oneself (see, for example, Salvatore, p. 408).

Fiscal federalism is also challenged by the theory of *localness*. This theory promotes a degree of redistributive activity at lower levels of government. It is argued that, in matters of redistribution, the spatial dimension is important: the desire to redistribute is influenced by the distance between the redistributing population for reasons of familiarity and more efficient results (Pauly, 1973). If people feel more strongly that they belong to the same community, they will be more inclined to promote social solidarity. Another challenge to the centralisation thesis refers to the significance of

differential preferences between regions, nations or states of a federation. For this reason, some argue that decentralisation may be recommended over centralisation.

4. American fiscal federalism and European subsidiarity in practice

When studying which level of social redistribution is most appropriate – centralised/federal or decentralised – it is worthwhile to consider the historical strategic choices that different nations or entities have taken. Clearly, the European Communities as a freshly established supra-national organisation chose a fundamentally different path from the US at crucial stages in the development of their respective social policy regimes.

a) American 'social federalism'

As mentioned before, United States social policies reserved a sizeable role for the federal - centralised - level, engendering a multi-tiered social architecture. This multi-tiered system actually combined federal social policy with a substantial role for the individual states. Illustrative in this respect is President Roosevelt's coining of this federal-state system as "a cooperative federal-state undertaking" when describing the Unemployment Insurance programme. A crucial task assigned to the federal level was to create incentives to states to develop their social programmes. With regard to unemployment insurance, Roosevelt's Committee of Economic Security noted that "so long as there is a danger that business in some States will gain a competitive advantage through failure of the State to enact an unemployment insurance law, few such laws will be enacted" (Pierson, 1995). To engender the necessary state action, the Social Security Act introduced a federal unemployment tax that would be levied only if the individual state failed to impose a state unemployment tax. The federal tax granted tax credit to employers who were already paying taxes under a state law that met federal requirements (these requirements also set minimum coverage and taxable wage base standards) (Rubin, 1990).

The political landscape behind the New Deal legislation demonstrates how US social policy resulted in shared federal-state responsibilities. A strong "Veto-coalition" of Southern Democrats, Republicans and certain business groups was concerned with retaining local control over social programmes in order to conserve the South's comparative advantage, being a black worker low-wage economy. Illustrative in that regard is the Southern politicians' accomplishment to ensure that the nationally administrated Old Age Insurance programme did not cover the self-employed, farm labourers and domestic servants, which effectively excluded three-fifths of all black workers (Quadagno, 1988). Even though certain programmes followed a nationalisation-track, not all programmes did so. The previously mentioned *Unemployment Insurance* was introduced as and remained a programme shared between the two levels of government (Rubin, 1990). As with previous programmes, Republicans, business lobbyists and Southern Democrats kept opposing successive nationalisation proposals in an effort to prevent generous standardised benefits from affecting the low-wage labour market. The same veto-coalition equally resisted nationalisation of *Aid to Families with Dependent Children*, a public assistance programme that succeeded the state- and local-level Mothers' Pensions programmes. At the same time, Northern liberal states favoured retaining state-level programmes⁶, as national reforms were seen as a threat to their better developed programmes, so that nationalisation would not improve their constituents' situation

⁶ This occurred when President Nixon proposed his Family Assistance Plan, which was in fact a national welfare system organised as a negative income tax with strong work incentives (Pierson, 1995).

(Pierson, 1995). Thus the federal and state levels kept sharing responsibilities to deliver welfare. The federal level stimulated activity by the states through the mechanism of matching grants. The fact that strong anti-federal 'movements' were simultaneously effective in keeping certain programmes at the state level (e.g. Unemployment Insurance and AFDC) or in resisting nationalisation until it suited their economic interests (e.g. Old Age Assistance until it became Supplemental Security Income) makes the US welfare state into a hybrid form of 'decentralised federalism'. Significant in that respect was the strong push for devolution of welfare to the state level during the 1990s, culminating in President Clinton's welfare reform of 1996. The ensuing devolution of welfare policies can be framed into general critiques on perceived excessive federal power. Critics protest against too much federal government: too many bureaucrats, regulations and spending, all of which entail an excessive burden of taxation. They further argue that the distance between the federal government and governed individuals is too great, which leads to a loss of Control and Accountability. Additionally, critics of excessive federal power fear that policymakers rely too much on cookie-cutter policies that do not take into account different local situations and preferences. They also argue that local officials are more responsive to local needs, and that local taxes are spent better than federal taxes. The 1996 welfare reform devolved even more responsibility to the states, through a system of block grants and maintenance of effort-obligations.

The fact that we find the bulk of US social spending at the federal level ties in neatly with a 'functional theory of federalism' which prescribes that 'redistribution' is best left to the national government while 'development' is a matter for both the state and local governments. If we look at the 'kinds' of expenditures the different levels of government have focused on, it becomes clear that, over the years, the US national (federal) government has increased its spending on re-distributive policies, while the state and local governments have focused more on developmental policies. Peterson calculated that the federal government's expenditure within the re-distributive sector more than doubled from 4.8 percent of GNP to 10.3 percent between 1962 and 1990. The bulk of this increase was geared to medical and social security programmes for the elderly, but welfare programmes also account for a portion of the rise (Peterson, 1995). Recently, while the expansion of the Earned Income Tax the weight of federal redistribution probably further increased. By contrast, the state and local governments focused on developmental policies, such as education, infrastructure and public safety services. As early as the early sixties, relevant state and local expenditure was more than twice as high as at the national level (Peterson, 1995).

Even though the theory of fiscal federalism approaches the reality of the US's choice to federalise social policy, it cannot be identified with US policy. Too many factors are in play that qualify the identification of fiscal federalism with the US. Even though most of the redistributive budget is spent at the federal level, crucial aspects of potential for competition between states remain at the state level, including essential parts of unemployment insurance and welfare.

We can conclude that the US applies a hybrid form of fiscal federalism. The US aspires to redistribution at the highest level, but continuous devolutionary pressure to keep social programmes at state level has hindered the full application of the classical theory of central redistribution (fiscal federalism). Nevertheless, if one compares US and EU social models, it is clear that, while many US programmes are implemented by states, they are subject to federal guidelines, federal incentives and federal financing. As a result, and contrasting with European welfare states, the US social model is characterised by a single architecture (one uniform social security system), by levels of social redistribution that are much more homogeneous across states, and by a significant pooling of resources for social redistribution at the federal level (federal government pays for a great deal of welfare programmes and most tax progressivity stems from the federal level).

b) *European subsidiarity*

When, in 1957, the French Prime Minister Guy Mollet called for a European harmonisation of social regulations and fiscal burdens, he was mainly concerned with possibly disastrous consequences of redistribution-related competition between member states. Europe, however, chose not to cover social matters in the Treaty of Rome. This political choice found justification in a report written on behalf of the ILO under Ohlin's presidency, in which it was argued that a harmonisation of social redistribution at the European level was not necessary to avoid a 'race to the bottom'.

Even though Ohlin echoed the intuitions later spelled out by the theory of fiscal federalism, he did not see them as a possible outcome in the European context.

Ohlin and his commission concluded in their report that the European federal level should guarantee the creation of a common market where the law of comparative advantages would provide profitable trade, i.e. a situation where each member state specialises in the production of those goods which it can produce better than the other member states. Like goods, certain social policies can influence the comparative advantages of states through their impact on the relative cost of producing goods. In such a context, there is no need to harmonise labour conditions because increased trade will increase welfare for all. Consequently, differences with regard to social protection levels were basically considered to reflect the income and productivity differentials between Member States. However, Ohlin explicitly assumed that a significant role was to be played by the trade unions at the national level, and that European governments would be sympathetic towards social aspirations, to ensure that social conditions would improve and not deteriorate. Trade unions had to preserve a natural link between wages and productivity to keep social security differences out of competitiveness issues.

Ohlin reconciled the benefits of a liberal common market with socially conscious national welfare states, arguing that "while the level of living of workers in high-wage countries would continue to rise, that of workers in lower-wage countries would tend to rise more rapidly. This tendency, however, is relatively weak and would not by itself lead to anything near equality in standards of living between countries... More important than this tendency in its effects on workers' living standards, we believe, would be the more rapid growth of productivity to be expected as a result of the more efficient international division of labour. This would be amply sufficient, in our view, when account is taken of the strength of the trade union movement in European countries and of the sympathy of European governments for social aspirations, *to ensure that labour conditions would improve and not deteriorate*" (ILO, 1956:86-87). Thus, Ohlin was confident that social improvements would follow from market integration spillover effects.

As a result of 'subsidiarity'⁷, there is only a very limited degree of social redistribution between the various EU member states: Europeans do not pool their resources in order to redistribute them among needy Europeans. The more redistributive European welfare states organise solidarity within fairly small and homogenous nation states only (so that some states are actually left without, for example, general and/or adequate assistance schemes; for overviews, see Sainsbury, 2001; Earley et al., 1996). Social protection in the US, by contrast, is nationwide. US data suggest that 35% of

⁷ I use the term 'subsidiarity' because: "the complexity of the multi-level European policy is not adequately represented by the single-level theoretical concepts of competing 'intergovernmentalist' and 'supra-nationalist' approaches" (Scharpf, 2000).

regional inequality in the US is offset by Federal income redistribution (see table below), which is of course considerably more than the amounts involved in the EU Structural and Cohesions Funds⁸.

Average redistribution and average regional inequality before redistribution

Country	Average Regional Inequality (Theil index before redistribution)	Average Regional Redistribution (Reduction in Theil Index)
Canada	0.0113	0.34
US	0.0076	0.35
Germany	0.0051	0.41
Australia	0.0026	0.54

Source: Ravishankar, 2003.

European welfare states developed within the frame of nation states. Consequently, quite substantial differences can be observed, not only in terms of the level of social redistribution, but also in the architecture of social protection. The three (or four) welfare models distinguished by Esping-Andersen are all represented within the European Union, as are the three major 'types' of social security (the Bismarckian, the Beveridgean and the demogrant types). Likewise, the extent of social redistribution is quite divergent. Measured on the basis of survey data, it appears that the extent to which income inequality is reduced through social redistribution ranges from between 30 and 38% in the Scandinavian countries, Belgium and the Netherlands, to between 23 and 25% in the UK and France, and to under 20% in Germany and Italy. The level of redistribution in the latter two countries approximates more closely to the level achieved in the US (around 18%) than it does to levels attained in the European member states where social redistribution is high (see table below).

Social redistribution in Europe and the US: pre and post tax and transfer Gini's

	Pre Tax & Transfer Gini	Post Tax & Transfer Gini	Reduction in Gini due to taxes & transfers
Sweden	32.7	20.2	37.9
Denmark	32.5	21.5	33.6
Finland	31.0	20.0	35.2
Belgium	33.7	21.6	35.6
Netherlands	37.5	26.0	30.6
Germany	32.2	26.2	18.7
France	39.4	29.4	25.4
Italy	35.7	31.3	12.1
UK	38.2	29.3	22.7
US	39.8	32.8	17.6

Source: Bradley et al., 2001.

The European social model has been characterised as: "a common commitment to social justice ..., the recognition that social justice can contribute to economic efficiency and progress ..." (Hemerijck, 2000: 173) or as an "extensive basic social security cover for all citizens ... and a more equal wage and income structure than in many other parts of the world". But is talk of one European social model justified given the huge differences between European welfare states? Besides differences in 'faiths' and 'the rather vague idea that the EU embodies a distinct social model' (Vandenbroucke, 2002), the most important distinguishing feature between the US and EU social models is 'subsidiarity': while, in the US, social redistribution is highly federalised and not so

⁸ Using cross-sectional regressions, Bayoumi and Masson (1995) estimated for the US that federal taxation reduces long-term income differentials by 22 cents out of every dollar.

developed, the EU has more extensive (albeit very different) social redistribution systems that are organised within comparatively small and homogenous nation states.

c) An ex post evaluation

Would European welfare states have fared well if, back in the 1950s, they had chosen the American 'New Deal' option? An ex post evaluation suggests the contrary: despite the absence of a supra-national social policy, all EU member states have succeeded in developing a strong social protection system. And conversely, American fiscal federalism produced less social redistribution.

Evidently, the comparison between US and European welfare state foundational history is skewed for several reasons. First, because Europeans are less mobile than Americans. Even if empirical evidence of the existence of welfare migration in the US is mixed, "policymakers (in the US) act as if migration is important" (Brueckner, 1998: 10). In Europe this is much less the case. Moreover, political sympathy and support for redistribution has probably been stronger in Europe than in the US. The impact of public opinion and pressure groups is generally regarded to be important in explaining why the US and European welfare systems are so divergent. A recent paper by Alesina cites behavioural elements, namely differences in the way Europeans and Americans think about redistribution, as a major cause of the divergent characteristics of their respective welfare systems (Alesina, 2003).

Nevertheless, there are good reasons to assume that the American hybrid form of fiscal federalism, too, was a hindering factor in the development of social protection: "A structural explanation of their incapacity to develop the necessary national standards and funding is America's decentralised federalism, which fosters a competitive race to the bottom" (Wilensky, 2002: 338). However, in the absence of a counter-factual, we can only hypothesise about the consequences that alternative strategic choices might have had in Europe and in the US. We can speculate, for example, that a pure, more profound form of fiscal federalism would have developed in the US if the 'veto-coalition' had had less political impact. However, given the heterogeneous nature of the US economy (low-wage agriculture in the South versus high-wage industry in the North), the 'smallest common denominator' in the field of redistribution would probably have prevailed. We can also try to imagine what the consequences might have been if, more in line with the evolution in Europe, comparative advantages would have played in a truly decentralised US model. Possibly the North would have had more in common with a (liberal) European welfare state, whereas the South might have developed a much more residual welfare state regime.

Likewise, we can speculate about alternative developments in Europe. Although the 1957 proposal for a harmonisation of social regulations and future burdens was not adopted, the theoretically and politically anticipated race to the bottom never materialised. Social redistribution in most European countries has clearly developed further than the American social model. What happened was exactly what had been predicted in the Ohlin report. While the structural differences regarding redistribution have grown in Europe, Member states have converged and are continuing to converge, albeit along different paths, towards similar levels of social redistribution.

This conclusion is at odds with the consensus in comparative literature that federalism (in the sense of decentralisation) is an impediment to welfare state expansion: "In fact, one might point to the federalism/social policy linkage as one of the very few areas of unanimity in the literature, with writers from all the main competing explanatory paradigms arguing that federal institutions are inimical to high levels of social spending" (Castles, 1999: 82). However, this conclusion is reached on the basis of studies comparing unitary with federal states. By contrast, my own conclusion is

founded on a rudimentary and unorthodox comparison of a federal state – the US – and an international organisation – the EU. As I pointed out in the introduction, I use this comparison only as a heuristic tool. Conclusions are therefore merely tentative and should not be generalised.

What can be said about the social-dumping argument in recent US and EU history? I have argued that, as far as Europe is concerned, evidence is mixed. Overall social expenditures do not point to any form of social dumping, though in some countries minimum benefit levels have decreased (sometimes dramatically) compared to average wages. The picture thus remains unclear. The same holds for the US. After devolution, the sceptics predicted a 'rush to the bottom' as a consequence of the shift from matching grant to block grant funding (see o.a. Peterson, 1995; Chernick and Reschovsky, 1996). According to Wiseman and Walker (2003: 42), there has been a '*subtle*' race to the bottom after devolution. However, Meyers, Gornick and Peck report that, after devolution, "states are *not* necessarily engaging in the often-predicted 'race to the bottom' following welfare reform. Relative policy effort appears stable across clusters of similar states over the 1994-1998 period, with the least supportive states continuing to provide very limited assistance and the most supportive states maintaining their policy commitments" (Meyers, Gornick and Peck, 2001: 458).

Opinions seem less divided with regard to the period before devolution. According to Pierson, "far and away the most significant retrenchment in AFDC occurred at the state level, where individual benefits are determined... Probably most important, concerns about interstate economic competition (both the need to keep taxes low and fear of becoming a 'welfare magnet') served as an *effective brake* on state generosity" (Pierson, 1994: 118-119). Peterson (1995) goes one step further in his book, describing a *dramatic* 'race to the bottom' prior to devolution. Paradoxically, this seems to suggest that the negative consequences of fiscal competitiveness were (are?) stronger under US social federalism than in the European subsidiarity model.

More generally, looking at the post-war 'worlds of welfare capitalism', we must also conclude that different versions of the social market economy have survived next to each other, and that there has been no tendency towards convergence of the architectures of social protection.

The belief that welfare states will (or should) converge is deeply ingrained in economics (, 1975 and 2002). Globalisation, modernisation and information-age technology have led more Wilensky and more observers to adopt a single peaked view of the world, a convergence towards one best practice. But there are arguments for diversified capitalism as well, as Freeman puts it: "Comparative advantage is a story of diversity; of gains that come from differing from one's neighbour, not from aping him." (Freeman, 2000: 4-5). Many observers conclude that the level of diversity between advanced economies has not decreased (Scharpf and Schmidt, 2000; Rhodes, *Welfare states and the EMU*; Krueger, 2000; Freeman, 2000; Scharpf, 2000; Soskice, Schettkat, 2000 and 2003). On the contrary, they believe that diversity remains possible within a globalised world. Diversity has been, and will probably continue to be, persistent among capitalist countries.

5. Lessons for the European Social Model

The (reassuring) conclusion thus far might be that a European supra-national system of redistribution is neither desirable, nor possible, nor required (Deleeck, 1992). From the US story we learn that federalisation can hinder welfare state development if parts of the federation differ too greatly economically. As we have previously mentioned, the conditions prescribed by Ohlin for a successful economic and social harmonisation of a group of countries are not attained today in Europe-15 and certainly not in the EU after enlargement: the economic and social differences between member states are simply too substantial to federalise social policy. Moreover, if the EU were to strive towards a harmonisation of social redistribution, the socially and economically least developed countries of the European South and East could form a 'veto-coalition', comparable to that in the US. Conversely, high-protection states might consider the common social protection levels to be insignificant or too low, again as happened in the US. Many of the Wisconsin reformers, for example, struggled to ensure that state autonomy would remain extensive so that Wisconsin could maintain its distinctive (and generous) programme (Pierson, p. 310). Looking at public opinions in Europe, one may expect the same to happen in Europe: citizens of the most advanced welfare states, in Scandinavia for example, will undoubtedly tend to oppose a Europeanisation of social policies most strongly (Mau, 2003).

But can we draw such simple and reassuring lesson for the future from the history of European and American welfare states? Probably not. There are, after all, various reasons why the parallelism between the historical genesis of the American and the European welfare states cannot be assumed to persist in the future.

A *first reason* is related to Pierson's distinction between 'old and new politics of the welfare states' (Pierson, 1996). The mission of welfare states today differs fundamentally from the mission at the time of their creation. It is no longer the case that the redistributive function of government needs to be developed. Today, in times of permanent austerity, welfare states need to reorient. This requires tough reforms that often go against vested interests. Consequently, Pierson argues that research on the 'golden age' of social policy is likely to provide a rather poor guide to the current period (Pierson, 2001). In their forthcoming book, 'Federalism and social Policy', Obinger, Leibfried and Castles quite rightly ask whether federalism supports or hampers the *new politics* of the welfare states. Their guess is that, "just as it was worthwhile for Member States to give up monetary sovereignty, there may come a time soon when they consider it worthwhile to trans-nationalise retrenchment by *regulating* common retrenchment corridors" (2004). While not resulting from a European retrenchment policy, the Belgian pension reform of 1997 can serve as a good example of how European regulations (in this case the Equal opportunity Guideline) can help governments to enact unpopular reforms. In fact pension age for women was increased by 5 years, without any commotion. This can only be explained by the fact that this reform was needed 'because of Europe'.

In the European context, there is a further aspect to take into account. The comparison that we made between welfare states in relation to subsidiarity, or as the case may be social federalism, cannot be generalised to a post-enlargement EU. After enlargement, the majority of EU countries will have strongly developed welfare regimes, while a small minority will be characterised by a still embryonic social redistribution. This context differs fundamentally from the situation at the birth of the American welfare state, when levels of protection were rather insignificant. At that time, the Southern States, because of their wage advantage, obstructed efforts to enhance the level of social redistribution for all states. A similar veto coalition among socio-economically weak countries within a hypothetical European supranationalism would not only imply obstruction towards a

higher level of social redistribution, but also a de facto decline in the level of social protection in the majority of stronger welfare states, which is of course a much tougher, though not entirely impossible, proposition.

A third reason why the conclusions drawn on the basis of the US-EU nexus cannot be readily applied to Europe today is related to the fact that the ability of EU countries to control the redistribution between member states is rapidly declining. First, because mobility within the EU may be expected to increase (while it may be the case that the independent development of national systems of redistribution was facilitated by the relative immobility of Europeans). The creation of a single European educational space could be an important catalyst in this respect. Second, because the influence of the supranational Europe is increasing, directly and – even more so – indirectly. There are many signs that the logic of a 'negative integration' (of the market) is increasingly at odds with the logic of a 'positive integration' (i.e. retention and further enhancement of social protection mechanisms). I quote the following examples: the Kohl-Decker ruling, in which the European Court settled two disputes relating to healthcare by giving precedence to the principle of free movement of goods and services; the conviction of Belgium for distortion of competition through a reduction in employers' social security contributions under 'Maribel'; the need to redesign the Flemish care insurance scheme because the residence principle which it incorporates is deemed to be incompatible with the EU's principle of free movement of workers; the proposal by the European Commission – albeit rejected by the European Parliament – with regard to the protected social status of dockworkers. And there are many more examples from other countries (pointing to the fact that national welfare states are becoming less able to develop or reorient independently (De Swaan, 2003; Leibfried and Pierson, 1995).

a) *Europe at a crossroads*

Europe is at a crossroads and now faces a twofold dilemma. Starting from the perspective that there is an evolutionary sequence in the development of citizenship rights (from civil rights over political rights to social rights), the development of a European social policy begs the question of whether the necessary democratic rights have already been realised. After all, "le welfare state n'est pas seulement un système ... pour transférer des biens. C'est un projet essentiellement politiques, si l'on entend par politique le projet collectif qui fait exister une société démocratique" (Schnapper, 2004). Clearly, in Europe such a 'common project' doesn't exist.. Figures show that that there is no unequivocal support for a European competence with regard to welfare (only 40% of the population in southern Europe are in favour of a Common European welfare policy, with about 30% support in the continental welfare states, and just 11% in Scandinavia, Mau, 2003). Europe also faces an institutional democratic deficit. This give rise to a dilemma that was formulated as follows by Offe: "In the case of purely negative integration, the threat is to the social welfare system ... In case of purely positive integration, it is the nation-state's established mechanisms for democratic legitimating that are imperilled" (Offe, 2000: 10).

The comparison between European subsidiarity and American fiscal federalism gives rise to a second dilemma. Although a Europeanisation of social redistribution would appear to be inevitable, the experience in the US suggests that federalisation can hinder, rather than enhance, the development of welfare states if parts of the federation differ too greatly. It is moreover safe to say that harmonisation is neither practically nor politically feasible. Inter-state differences are too stark and, frankly, there is a lack of political will. Moreover, we learn from US experience that serious practical difficulties may arise in steering a social federation centrally. Examples are the tough management of federal grants to the individual states and difficulties to check compliance of Unemployment Insurance rules with federal standards. Additionally, a federal system misses

opportunities for innovative practices – a policy goal now pursued by the US in the framework of devolution.

b) *The Open Method of Co-ordination and beyond*

So what (if any) European social policy should we pushing for? My recommendation would be to try, by means of the Open Method of Coordination or OMC, to arrive at binding agreements regarding minimum social standards. The guarantee for all European citizens – within their own nation-state – of a proportional adequate minimum income protection seems to be a good starting point.

The actual approach of European social policy is articulated around the 'convergence of objectives'. In order to achieve this goal, the Open Method of Coordination (OMC) is applied. This is a process of defining objectives, peer review and identification of 'best practices'. The method is applied in employment policy, pension's policy and in relation to social inclusion. Objectives are quantified through 'social indicators'. The OMC and the social indicators relate exclusively to policy *results*, not to the actual policies chosen to reach the common objectives. In other words, the member states are free to choose a path towards common goals.

The leading thought behind this approach differs significantly from the perspective that was popular in the 1990s. Instead of emphasizing the aspect of 'convergence' of concrete policy objectives, e.g. in relation to the formulation of minimum norms for social benefits, the focus is now on convergence of policy outcomes. In this context, it is not surprising that the EU Council Recommendation of 24 June 1992 on common criteria concerning minimum income guarantee and social assistance in social protections schemes (92/441/EEC)⁹ has faded into the background, as has the political debate concerning the question of the necessity and desirability of common standards for social policy.

However, if developed welfare states want to survive while enhancing social protection in the less developed states, agreements on such issues will have to be made binding in the future. European welfare states can no longer assume that they will be able to develop unhindered, as once used to be the case. For that matter, with the necessity of reforms and adaptations to new kinds of risks and needs, there is a danger that developed welfare states, too, will lose sight of the significance of social redistribution and adequate minimum protection. As is apparent from Table 1, this has actually been the case in some so-called 'strong welfare states'. The single currency, the side-effects of expanding European regulations on free movement of labour, capital, goods and services, and most probably the (albeit slow) development towards a single European labour and education market necessitate binding agreements.

So, from a practical perspective, what are the options for progressing towards this objective? The OMC could provide a starting point (see for example Vandenbroucke, 2003; Visser, 2001; Pochet, 2004; Telò, 2004; Rodrigues, 2002). It offers the advantage of inducing an organic integration process and of solving the dilemma between 'subsidiarity' and 'social federalism'. However, it should be noted that the OMCs that are already in place have not been very successful. In the case of the OMC on social inclusion, this is primarily due to the fact that the output indicators – however important they may be – are not really operational for policymakers. Seven lead indicators were adopted covering the broad fields that have been considered the most important contributing factors to social exclusion: financial poverty, income inequality, long-term unemployment, joblessness, low

⁹ PB L245 of 26 August 1992.

educational qualifications, low life expectancy and poor health (Atkinson, Cantillon, Marlier, Nolan, 2002). These indicators are an important tool for evaluating a country's level of social development and for assessing the impact of policy. The indicators are reported in the Joint Reports on Social Inclusion (European Commission, 2002 ad 2004). These reports, which constitute a European social scoreboard, reveal huge differences between member states. But the question remains whether they will set into motion the necessary cooperation of social policies. To quote Atkinson, "the OMC is often dismissed as 'cheep talk'. There are no policy institutions such as the European Central Bank. There are no financial penalties as under the stability and Growth Pact. Member States can ignore the social indicators. The freedom of choice allowed under subsidiarity may be largely illusory if policy is dictated by budgetary considerations. We will have to wait if this is true, ..., but there are certainly good reasons to suppose that Member States will take seriously the regular two yearly review of progress towards social inclusion, and their performance on the social indicators" (Atkinson, 2004: 16). I, however, am less confident. After all, the level of poverty or income inequality is affected by a broad range of social, economic and demographic factors. Therefore, policy measures have – at best – only a marginal impact on Gini coefficients or on average poverty-risks. This is why policymakers tend not to feel called upon. Judging by the Belgian experience, this is probably the reason why neither the social partners nor national parliament nor the media have devoted any attention to the issue¹⁰.

The modest success of the OMCs dealing with social protection is in part due to its fragmentary nature and to the fact that no agreement can be reached on the relevant output indicators. This is why the recent communication by the Commission on "the streamlining of current disparate actions linked to social inclusion and pensions and, in time, cooperation in relation to healthcare and 'making work pay' into a single Open Method of Coordination' and to 'report on the advisability of simplifying and streamlining the various strands of work on social protection into a coherent framework within the Open Method of Coordination'" is an important step. If the OMC on inclusion could be coupled with an OMC on social protection, i.e. if a political link could be made at the European level between such output indicators as poverty, income inequality and unemployment on the one hand and social protection on the other, then the political impact of European peer review might be much greater than it is at present.

¹⁰ See for empirical evidence that the OMC (as yet) does not live up to its own democratic ambitions, de la Porte and Nanz (2003).

6. Conclusion: towards binding agreements on a guaranteed minimum income?

Coupling the OMC on social protection with that on social inclusion could clear the path towards politically binding agreements on such policies. More specifically, if a link is established between the OMC on social inclusion and the OMC on social protection, an agreement on a common (but proportional) guaranteed income floor in and out of work would follow.

Returning to table 1, it could be argued that if such a European guideline -incorporated into an OMC - had existed, minimum protection in some high protection countries like the Netherlands, Sweden, Norway and Belgium would, most likely, not have been eroded to the extent it has done over the past decade or so. These welfare erosions can hardly be regarded as an inevitable consequence of globalisation. After all, some countries have succeeded in escaping the trend. It does however indicate that all those who are concerned with the future of social redistribution could well use some social benchmarking by Europe. For the less developed welfare states, such binding European agreements can serve as a lever for the development of an adequate minimum protection. For the most developed welfare states, such agreements can help guard against a risky erosion of minimum protection. After all, insofar as minimum levels of protection are formulated proportionally (i.e. taking into account average wage and GDP), such agreements need not imply that the standards set are too low (and thus insignificant) for countries that already enjoy high levels of social protection.

This conclusion implies that - contrary to the US system – personal redistribution in Europe continues to be organised within the different member states, but with binding guidelines about minimum protection standards. Redistribution between nations could then be achieved through structural funding of development policies in infrastructure, education, employment and public services in poor regions and nations.

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