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What do Unions Do to the Welfare States?

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A Report for the Fondazione RODOLFO DEBENEDETTI

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> "Despite their significance, the forms of dialogue used and the routes followed by the reform process are generally not well known. In a way they are the hidden face of recent pension reforms. Most of the work, especially international comparisons has concentrated on the purely technical aspects (...). The decision-making aspects have largely been left in the shadows, yet they are a major factor in the implementation of reforms and the long-term viability of systems. (Reynaud, 2000: 2)"

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Introduction

The previous quotation from Reynaud (2000) provides the motivation for the research described in this report. In the economic, sociological and political analysis of welfare systems and their reforms, little emphasis has been traditionally given to the decision making process, and on the specific roles of the various actors in implementing reforms. This report partially fills in this gap, and investigates the interactions between trade unions, welfare systems and welfare reforms.

Historically, trade unions have played a prominent role in the provision of insurance to workers and their families. Indeed, the function of protecting employees against social risks has often anticipated the role of unions as workers representatives in bargaining over wages and work conditions. While unions have a long established role as an institution that provides voice and protection to workers, the economic literature has shown that these activities can be efficiency enhancing, in as much as insurance markets are imperfect and/or incomplete, and non-competitive forces in the product markets are sizable. Further, trade unions have also shown concern for wage inequality, and have promoted redistribution policies in ways that go well beyond the traditional “wage compression” paradigm.

Nevertheless, unions do enjoy a monopoly position in particular labour markets, and without appropriate incentives and countervailing forces, their activities may adversely effect the economic performance of a country. Thus, unions involvement in the welfare state may simply reflect the monopolistic face of trade unions, and consist of lobbying for generous policies to the exclusive advantage of union members. The use of selective incentive may be implemented under different formats of the organization of labour – entailing different degrees of union coverage and union fragmentation – and may be prominent when unions are involved in self-administration of welfare benefits, and/or when they play a key political role in welfare policy decision-making. Trade unions seem affected by a “seniority bias” both in their wage bargaining and in their choices over social welfare policies. This seniority bias may, in turn, have negative effects on employment, and ultimately on the membership structure of unions themselves.

This report discusses some policy issues that arise in this context. The overall theme is the policy dilemma created by the many different activities of trade unions in the field of welfare provisions, notably pension policies and unemployment protection. Throughout the report a tension emerges between the role of unions as insurance providers, as institution that facilitates agreements between different parties, and as rent-seeking monopolist. By making use of an interdisciplinary approach, involving economic theory, political science and statistical analysis, we are able to rationalize a set of distinct features of the interaction between union activities and union structure on the one hand, and welfare arrangements and welfare developments on the other hand.

To our knowledge this is the first attempt at laying out a comprehensive description of the possible effects of trade unions on welfare regimes and social expenditure trends. This report builds on uneven foundations, since there exist few contributions that bring together the industrial relations and economic literature. Nevertheless, we believe that this report shows that the benefits of cross-fertilization far outweigh the costs of bringing different methodological approaches together when dealing with this topic.

Indeed, the report uncover aspects of union behavior that seem to have been overlooked by models that depict trade unions concerned only with industrial relations outcomes. In particular, we establish a new important link between the traditional rent-seeking activities of unions, and some "political economic activities", such as taking direct responsibility in the provision and administration of insurance, or taking long-tem commitment in welfare policies involving intergenerational transfers.

While unions may probably exhibit a “static-efficiency” role in providing insurance, they are likely to feature a “dynamic inefficiency” role, in the sense of treating differently different generations of workers. The activities of unions which best conform to this view are the implementation of “soft landing plans” in public pension systems, widely observed in Europe. More generally, unions tend to preserve the status quo when it comes to cutting pension benefits or reducing generosity of pension provisions or when a retrenchment process of welfare spending is to be implemented. The cost of these dynamic inefficiencies may be accepted by younger generations as long as an intergenerational contract can be enforced, whereby unions guarantee that the status quo will be preserved, and unions are credible in their commitment. In this intergenerational implicit pact the unions could play a key role because they are long-lived agents, certainly lasting longer than many governments.

In the light of the recent trends in population aging, most OECD Member countries are under pressure to reform their social policies in order to stabilize welfare costs. Winning the support of unions in welfare reforms may be the first step to achieve this goal. But such role also requires that the trade unions become aware of the costs of social protection expenditure for the whole economy and the potential inefficiencies and distortions that may result from their actions at a micro-economic level in the labour market.

This report is organized as follows. **Section 1** shows that there are important correlation between the unions strength and activities and welfare outcomes. The attempts to provide a taxonomy of the large differences across countries in union strength and social expenditure, by simultaneously making use of both labour relations and political-economy categories as well as welfare categories and social spending measures. One dimension of our analysis provides four clusters of groups of countries, which share common features in terms of union strength and bargaining traditions and in terms of welfare arrangements. At one extreme we place Nordic Countries, which have a long standing tradition in universal protection and high union density, while at the other extreme a cluster of Anglo-Saxon countries emerges as characterized by low social protection expenditure and low union density. Continental countries and Southern countries lie somewhere in between. This classification is by no means exhaustive or complete and important differences emerge both within each group and in other dimensions of union activities, particularly in their role as market institutions. We cannot explain cross-countries variability without referring to the industrial model that each state adopted and, most importantly, to the different routes through which unions influence welfare policies.

Section 2 develops the relationship between union actions and welfare outcomes. The presents an economist's perspective, and presents an abstract economic model that offers as analytical framework for investigating the behavior of unions in the welfare state. Further, it presents real world counterpart on the empirical implications emerging from the model. In light of the stylized facts presented in Section 1, which confirm the involvement of unions in pension arrangements along several dimensions, Section 2 takes the provision of old age insurance provision as a natural example. Economic theory stresses the role of unions as insurance providers, and looks at a full bargaining set up where unions have influence on current wages, pensions and employment outcomes. A novel feature of the description of union behavior is that it also accounts for heterogeneity of union members, by distinguishing senior workers from junior workers. This clearly brings out the effects of the seniority bias affecting union decisions in wage bargaining, and also in pressing for generous pension policies. A review of the existing literature on unions and pensions based on microeconomic empirical research is provided along with some fresh evidence on the interaction between unions and welfare at a macro level.

Section 3 provides a detailed account of the position of unions over pension reforms. We regard this aspect of union activities as a major indicator to establish whether unions have a truly solidaristic approach in negotiating reforms or whether they appear to be driven mainly by internal membership considerations and by a strong seniority bias. We provide both examples of situations where unions oppose welfare-restructuring reforms by effectively preventing their implementation and examples where unions negotiate over policy changes by taking a long-term view.

Section 4 explores the involvement of unions in the provision of unemployment insurance. We present theoretical considerations, policy arguments and empirical evidence in the light of a particular unemployment insurance arrangement known as the Ghent regime. This form of unemployment provision is adopted in some Nordic countries and it is an interesting example of self-administered insurance by the trade unions in contrast with a compulsory universal system. It is an interesting economic example because the provision of unemployment insurance in a Ghent regime has the nature of an "exclusive service", but this is usually coupled with a subsidy by the government financed through general taxation. Hence the policy questions we ask in the introduction, related to the traditional trade-off of union activities, can be addressed in this context. Is the Ghent unemployment arrangement efficient in the sense of providing the correct incentives to job search? Do unions internalize the cost of the negative effects that financing the scheme may entail? **Section 5** concludes.

1. Unions Involvement in the Welfare State

Trade unions have been a major force in the development of modern welfare states, and they still assume multiple roles in shaping and administering welfare states across the world. Historically, trade unions developed mutual insurance as part of associational self-help for lack of private or public insurance. At the same time, unions mobilised together with allied parties for the expansion of social rights. Increasingly, many of the protective functions that unions had experimented with were taken over by the state or at least regulated by public policy. In some publicly mandated schemes, unions (or worker representatives) gained an institutionalised role in their administration. In some rare cases, unions were able to maintain their administrative control over voluntary insurance, while receiving state subsidies. This is still the case for unemployment insurance in some Nordic countries. Furthermore, in addition to publicly mandated social security, unions often negotiated supplementary occupational benefits (in particular, if public benefits only provided for a basic security level). We will focus on the case of publicly mandated and private occupational pension as well as state and voluntary unemployment insurance as two cases for studying the different roles unions can assume in shaping and administrating social insurance. In this section, we will discuss the different ways in which unions can influence welfare policies. In particular, we will distinguish among the following four dimensions of union influence: (i) *unions as political movements*, (ii) *unions and self-administration*, (iii) *unions and pensions*, and (iv) *institutional participation and political veto points*.

The role of unions in welfare policy making and implementation varies across countries, reflecting different political traditions and institutional legacies. On the continent, many welfare states followed the Bismarckian principle: social insurance was not only based on payroll contributions paid by employers and employees, but also on their representation in the self-governing social insurance scheme. On the other hand, in the Berveridge tradition of state provided social assistance to the needy, unions would not be directly involved in the administration of the basic pension and other welfare schemes. In order to capture these pronounced cross-national differences, we focus on a specific group of European countries in this section: Austria, Denmark, France, Germany, Italy, the Netherlands, Sweden and the United Kingdom. This broad set of countries provides an interesting variation not only in terms of union influence in the welfare state, but also in terms of welfare regimes (Esping-Andersen 1990). Following the classification of welfare regimes applied by Bertola, Boeri and Nicoletti (2000), our set of countries represents the whole spectrum of European Welfare regimes: namely *Nordic* (Sweden, Finland, Denmark), *Continental* (Austria, Belgium, France and Germany), *Anglo Saxon* (UK and Ireland) and *Southern* (Greece, Italy, Portugal and Spain), whenever possible a wider set of countries will be considered including also the USA, Canada and Japan.[1] This section aims at mapping union involvement in public and private social protection across different welfare regimes. We will first analyse the relationship between union movements and welfare regimes at a general level, and then look at the different dimensions of union influence.

1.1 Unions and the Welfare State Development.

When studying the development and scope of modern welfare states, social expenditures are commonly used as the best overall indicator for the economic resources committed to social protection[2]. The common socio-economic explanations for the long-term increase and the cross-national variations are related to three main factors: demographic structure, labour market and the level of economic resources (Peracchi, 1999). Thus, pension (and health expenditures) are expected to rise with aging population. Also expenditures on unemployment and early retirement have increased with aggravated labour market conditions. And at a global scale, one can find that the more wealthy a nation, the higher social spending. Yet these functionalist factors can only explain a part of the long-term growth, and even less of the cross-national variations in social protection. A number of historical contingencies, institutional legacies, and socio-political factors have led to historically developed differences in social protection, which go beyond the size of the welfare state and include societal choices about who provides social protection and under what conditions.

At the basis of the differences in welfare regimes are two distinct principles of social protection: on the one hand, the maintenance of living standard, that is earning protection,

[1] This classification was based on each country's position in its ability to: help the poor, reducing inequality, and increasing rewards from labour market participation. See Bertola, Boeri and Nicoletti (2000).

[2] According to Eurostat – Statistical Office of the European Community – social protection is social intervention from public or private bodies to relieve households and individuals of various social risks, provided that it is not unrequited and it does not take place under individual arrangements.

and on the other hand, the eradication of poverty, that is, to guarantee a minimum income . While the first mechanism is based on distribution within a social risk pool and reproduces earnings inequality, the second mechanism is based on redistribution. The *Bismarckian* view broadly corresponds to the provision of earnings related benefits (typically characterized by relatively high average replacement rates), while the *Beveridgean* view places more emphasis on the safety net aspect and typically adopts flat-rate benefits. These were traditionally means-tested but have become often citizenship rights. The continental welfare states, including to some extent the Southern countries, conform to the Bismarckian approach, at least in respect to pension policies. The Nordic welfare states and typically Anglo-Saxon countries conform more to the Beveridgean basic pension idea. Coverage is universal, including all retirees and is not related primarily to labour market activities. However, also in these universal welfare systems, supplementary earnings-related pensions coexist, be it as voluntary occupational pensions and / or mandatory state pension schemes. Therefore, in practice, the replacement rate of supplementary pensions on top of Beveridgian basic pension may also vary according to contributions, like in the case of Bismarckian social insurance.

A first glance some general indicators on welfare-state regimes (see Table 1.1) indicate some clustering, though there are also significant deviations within a cluster. Esping-Andersen´s measure of de-commodification (1980) summarizes the generosity and comprehensiveness of social security for three social risks (old age, sickness, and unemployment), and serves as the basis for his clustering of countries[3]. With the exception of Finland, all Nordic universalistic welfare states show—as expected—the highest scores. They are followed at a distance by the „Christian-Democratic“ social-security states of Austria, Belgium and the Netherlands, while Finland, Switzerland and Germany, as well as France, rank as the third group. The Anglo-Saxon liberal welfare states (Britain and Ireland), and the Latin-rim residual welfare states of Italy, and probably Portugal and Spain (for which no data is given), are at the bottom of the index, as the regime analysis assumes. Thus only Finland and France are critical borderline cases: the former being a late-comer in respect to the other Nordic welfare states, and the latter being a mixed case of a Bismarckian social-security state that lagged behind some of the Christian-Democratic ones and of the more familist Latin welfare states.

[3] De-commodification is the extent to which individuals uphold a socially acceptable standard of living, independently of market participation. It is essentially a measure of the generosity of the safety net available to non-employed individuals.

Comparing the current OECD data on social expenditure (% GDP, 1993), we find a similar pattern: the Nordic welfare states spend considerably more than Continental social-insurance states, though the Netherlands and reunited Germany spent as much as the Scandinavian laggards (Norway and Denmark). Austria, Belgium, France and Italy come third, while the Anglo-Saxon countries, but also Switzerland, Spain and Portugal lag behind. Cross-national variations can also be found in respect to the form of financing and the type of expenditures. The relatively extensive Nordic welfare states are largely financed by general taxation, with some social insurance contributions from employees and especially employers. The more moderate Anglo-Saxon welfare states have also a relatively small share of social expenditure being financed by mandatory employment-related contributions. In contrast, the Continental social-insurance states do follow the Bismarckian model more closely—more than half of current expenditures are financed by payroll taxes. Yet not everywhere are the burdens shouldered equally by the two sides of industry (the Dutch workers and Belgian employers contribute more than the other side). Finally, in the Latin welfare states social insurance contributions are also important, especially in France. Like in Belgium, mandatory employer contributions exceed the share of workers in payroll taxes.

Comprehensive and efficient insurance against social risks are rarely provided by private market, thus welfare sates have intervened by compulsory social insurance. In economic theory, the rationale behind the missing insurance markets paradigm is the existence of informational problems affecting the contracts that each worker should sign with a private insurance company. Once publicly mandated programmes are installed, they are likely to crowd out private arrangements at least for the basic benefits provided under the state plan. For the position of unions, a mandatory programme is more beneficial than a voluntary insurance since it provides comprehensive coverage, thereby leading to a larger risk pool and including those that might not be capable of supporting themselves. Since such publicly mandated schemes are involuntary, redistribution is possible, while in a voluntary scheme those that are net payers may leave when forced to subsidize benefits of others. On the other hand, unions might consider providing social protection as a selected incentive which would be beneficial for union membership and strengthen their role. However, the odds for self-help are usually high: the risk pool (unionization rate) might be too small, membership fluctuation too large, and the risk too cyclical (e.g. unemployment). Occupational benefits could be a second best (if not the best) solution if unions are strong enough to negotiate such schemes on a comprehensive basis, while in the case of voluntary, unilateral fringe benefit by employers unions would have no say at all. Thus we would expect that for the role of unions in welfare states, the organization of labour in general as well as the character of employer-union relations shape the opportunity structure for unions to influence social protection, whether publicly mandated, collectively negotiated or unilateral voluntarist schemes.

Table 1.1: Welfare States in Western Europe (1990s).

	Decommo-dification 1980s	Soc.Exp. %GDP 1993	Contributions (% Soc.Exp.) Employees 1994	Employers 1994	State 1994	Old age % Soc.Exp 1993	Unempl. % Soc.Exp. 1993
Country	(1)	(2)	(3)	(4)	(5)	(6)	(7)
North							
Denmark	38.1	31.0	4.2	1.2	94.7	27.5	24.2
Finland	29.2	35.4	4.4	28.2	67.4	40.1	19.0
Norway	38.3	29.3	11.8	20.0	68.2	31.9	9.0
Sweden	39.1	38.0	2.6	33.0	64.4	33.9	15.3
Centre							
Austria	31.1	25.8	25.2	28.2	46.6	56.4	6.9
Belgium	32.4	*27.0	18.8	34.7	46.5	*43.4	*15.2
Germany		28.3	23.7	27.6	48.6	45.9	15.3
(West only)	27.7	(24.7)				(48.1)	(11.5)
Netherlands	32.4	30.2	41.5	9.9	48.6	44.4	12.5
Switzerland	29.8	*20.6	18.8	17.9	63.3	*50.4	*6.1
West							
Great Britain	23.4	23.4	10.6	14.6	74.8	39.3	7.6
Ireland	23.3	20.1	9.3	16.0	74.6	29.4	24.3
South							
France	27.5	27.3	21.5	43.3	35.2	44.1	11.6
Italy	24.1	25.0	11.0	34.7	54.3	60.6	8.3
Portugal		16.3	20.2	30.4	49.4	51.8	10.6
Spain		22.5	10.8	42.6	46.5	46.2	19.1

Source: (1) Esping-Andersen (1990): 52; (2), (3-6): own calculations from OECD (1997); (4-8): OECD (1996).
Note: Soc.Exp.: Social Expenditure (OECD definition). (1) Decommodification index (1980): combined additive measure of benefit quality, coverage, and conditions for pension, sickness, and unemployment benefits (see source p. 54). (2-4): Contributions calculated from social security and tax income (1994) and social expenditure (1993); (5): state: 100%-social contributions. (6): Old age including survivors and disability insurance. (*) 1992

A comparison of western European industrial relations systems according to qualitative and quantitative indicators reveals some clustering into similar four regimes as in the case of welfare regimes (see Table 1.2). First, in terms of the organization of labour, we find systematic differences with respect to cleavage structures and mobilization patterns. When we look at the number of main confederations, and the nature of splits within the labour movement, we find important differences. The Nordic countries all have one Social-Democratic labour confederation that is organizing the blue-collar workers (largely in industrial unions) in particular, while white-collar workers have funded some rival or separate peak organizations. The British and Irish union confederations, on the other hand, are the only peak associations, though a relatively weak umbrella for a variety of craft, general and industrial unions also exists. Some of these unions are affiliated to the Labour party. Political and religious splits are particularly pronounced in the Latin labour movements. But these cleavages also have some residual importance in the Benelux countries and Switzerland, while Austria and Germany have overcome these since the end of Fascism through non-partisan unitary confederations.

In respect to the level of unionization, measured by union density, Scandinavian countries are leading the ranks in steady, high unionization levels, while the Roman labour movement has relied more on cycles of political mobilization. The Continental labour movements have a medium level in membership mobilization—Belgium and Austria rank higher than Germany, the Netherlands and Switzerland. Britain and Ireland had somewhat higher levels in the past, but in particular Britain has witnessed a dramatic decline in unionization since the Thatcher government introduced new labour legislation. Partly as a consequence of the concentration or fragmentation and strength or weakness of unions, important differences exist in respect to strike propensity and volume of industrial conflicts: polarized Latin and Anglo-Saxon labour relations, but also more recently Scandinavian countries, show a higher level of strikes and lockouts compared with the Continental social partnership countries.

On the side of capital, we also find considerable differences in organization, although for less political reasons. Some countries, in particular Germany and Sweden, have specialized employer peak associations that are relatively centralized and well-organized, whereas in other countries general business associations combine labour market and producer interests within their ranks. A low level of membership, weak centralization, and often paternalistic union opposition is particularly problematic in the Anglo-Saxon and Latin industrial relations systems. As a consequence, collective bargaining covers less workers, which is particularly the case in Britain. While in the Scandinavian countries both employers and unions are well-organized and thus can enforce voluntary collective agreements throughout the economy, thus hardly needing state intervention, this is not the case elsewhere. Particularly in Latin industrial relations, such state intervention can be crucial in extending collective agreements that have been negotiated by relatively less-organized and unrepresentative bargaining partners to larger s of the economy. In Britain, however, no legal extension mechanisms are at disposal—which is particularly harmful given the increased decentralization of collective bargaining and the lessening recognition of unions at the workplace level.

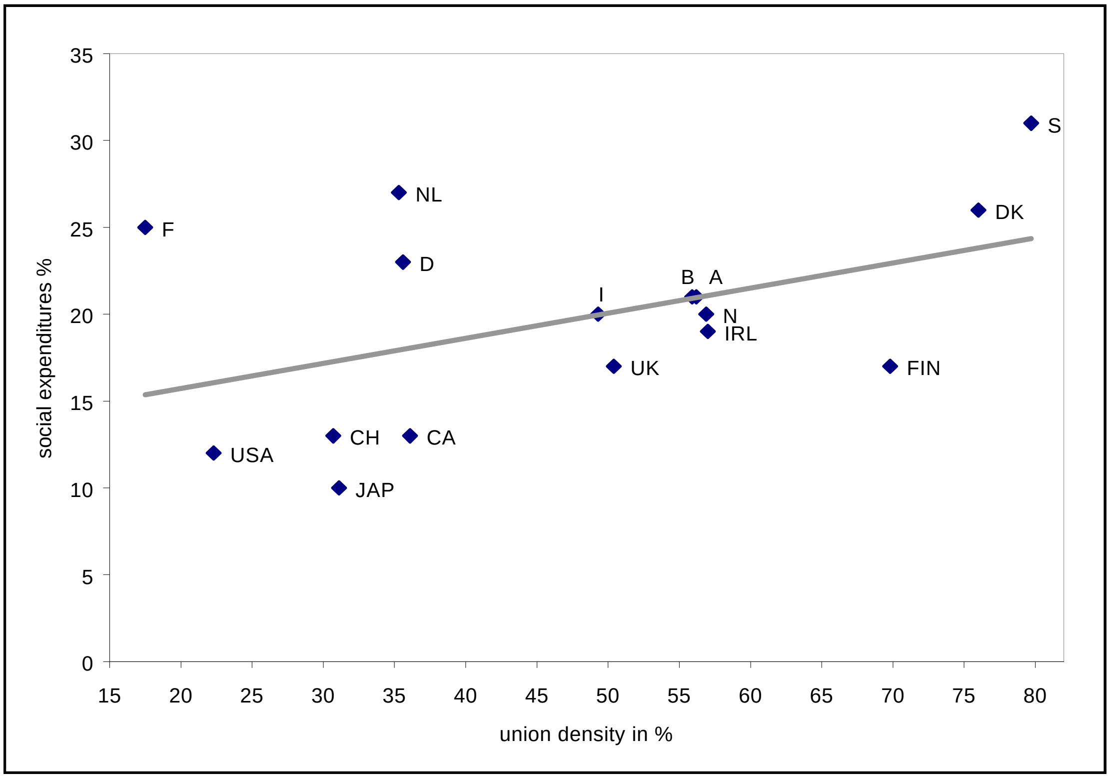
Table 1.2: Industrial Relations in Western Europe (1990s).

	Organized labour			Organized capital		Collective Bargaining		
	N of conf.	Main cleavage	Union density	Main peak	Empl. covered	Bargaining level	Barg. coverage	Erga omnes extension
Country	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
North								
Denmark	1.7	collarline	71.4	EA	90-100	sector	>80	Voluntary
Finland	2.0	collarline	72.0	BA ind.	60-70	national	95	Mandatory
Norway	1.8	collarline	56.0	EA	70-80	national	75	Voluntary
Sweden	2.0	collarline	82.5	EA ind	90-100	sector	83	Voluntary
Centre								
Austria	1.0		46.2	BA	100	sector	98	Mandatory
Belgium	2.2	religion	50.1	BA	80-90	nat./sector	90	Mandatory
Germany	1.4	collarline	32.9	EA	80-90	sector	W. 90	Mandatory
Netherlands	2.3	collar/rel.	25.5	BA	70-80	sector	81	Mandatory
Switzerland	2.5	collar/rel.	26.7	EA	ca. 50	sector	53	Mandatory
West								
Great Britain	1.4	indep.	39.1	BA	20-30	firm	47	None
Ireland	1.2	indep.	50.8	BA	30-40	nat./firm	>70	Mandatory
South								
France	4.2	political	10.8	BA ind.	30-40	sector/firm	82	Mandatory
Italy	2.5	political	38.8	BA	70-80	sector	70	None
Portugal	2.0	political	31.8	BA ind.	30-40	sector	79	Mandatory
Spain	2.3	political	16.1	BA	60-70	sector/firm	>70	Mandatory

Source: Ebbinghaus and Visser (1997),).
Notes: (1) Number of main confederations (weighted by share); (2) Cleavages: religious, political, and / or collarline (white vs blue-collar); (3) Density: union members as percentage of dependent labour force; (4) major peak employer association: Ind.= industry only; EA= employer association proper, BA= business association (employer and trade association); (5) Employees covered: percentage of employees in organized firms; (6) Level: main level of collective bargaining; (7) Coverage: share of employees covered by collective agreements; Germany (West), East: 63 (1992); (8) Extension: erga omnes extension of collective agreements, mandatory for all firms or voluntary.

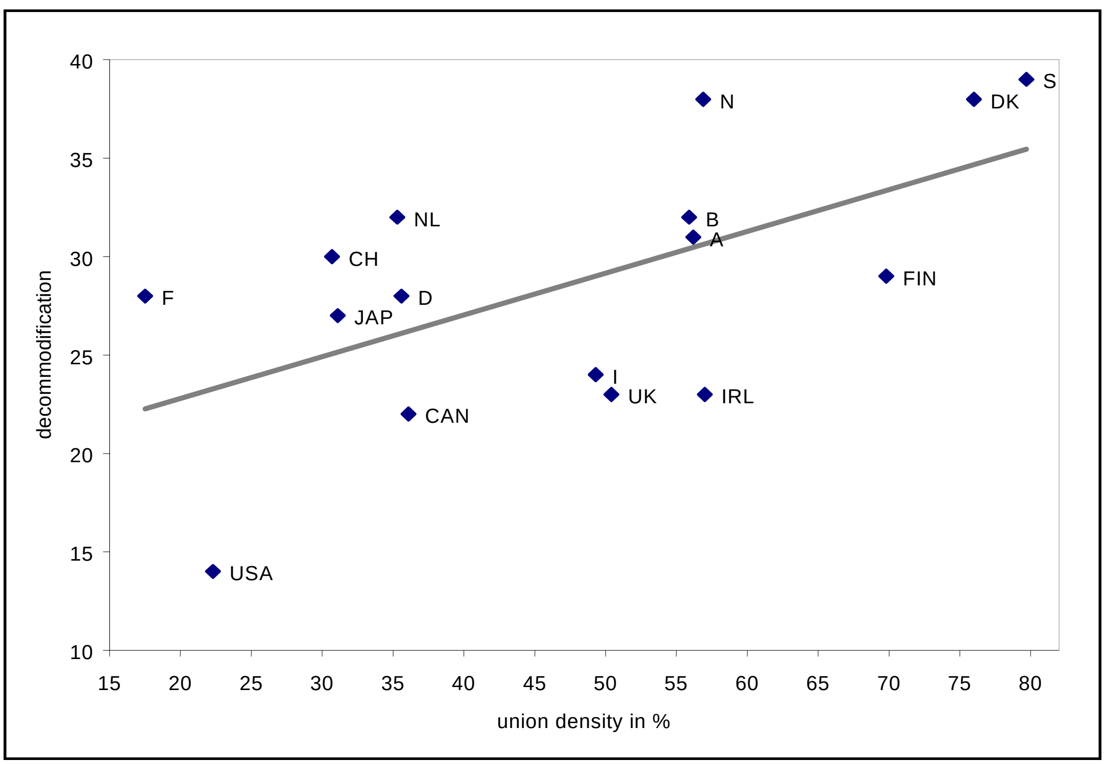
One aspect of the relationship between welfare regimes and labour relations can be explored by looking at the correlation of unionization and welfare state indicators. Historical accounts and time series models have found that indeed strong union movements and the expansion of the welfare state have gone together (Esping-Andersen 1990). This can also be seen from the two scattergrams that plot net union density with welfare state indicators across OECD countries for 1980. In many countries, 1980 is the year for which Esping-Andersen (1990) provides his decommodification indicator, but it marks also a turning point in postwar union density (Ebbinghaus and Visser, 2000). When looking at social expenditure (% GDP) and decommodification cross-nationally, we can find some relationship between union density and welfare state development. The Nordic high-density countries (Sweden and Denmark) are the best welfare performers, while the low density country (USA) is also the worst performer. Yet the relationship is not as clear, some countries like France, have well developed welfare states, while union density is much lower than would be expected. In these cases, there seem to be other historical, political and other factors that account for the particular welfare regime. Thus, institutional factors intervene, for instance, bargaining coverage is in France relative comprehensive despite low unionization due to the intervention of the state via *erga omnes* extension of collective agreements. Such state extension had made collectively negotiated occupational pensions mandatory for French employees, something the weak and divided French unions would not have been able to achieve by themselves.

Figure 1.1: Union density and social expenditure (1980).



Source: Huber and Stephens (1999), OECD (1994).

Figure 1.2: Union density and decommodification (1980).



Source: Huber and Stephens (1999), Esping-Andersen (1990), OECD (1994).

1.2 Unions and Membership Structure

Historically, union movements gained strength for promoting welfare state development on the basis of their rank-and-file in both the political arena (members as potential voters) as well as in industrial relations (as potential strike supporters). Indeed, the expansion of welfare states has been linked to the rise of labour movements and their increased organisational power (Esping-Andersen, 1990). However, union movements have come under increased pressures over the last two decades with the onset of mass unemployment, decentralizations of collective bargaining, flexibilization of employment contracts and social changes. Thus, over the past decades there has been an increasing divergence in union density across countries. While most unions lost considerable in membership and union density (see Graph 3), there is an important exception in the case of *Nordic countries*, such as Denmark and Sweden, which profited from *union-led unemployment insurance*. Very dramatic decline in unionisation occurred in the United Kingdom since the 1980s, but also union movements in some of the continental countries, for instance, the Netherlands, showed long-term decline. While about four out of five Scandinavian workers are unionised, this is the case only for every third Italian and British worker, every fourth German and Dutch worker and merely every eleventh French worker (Ebbinghaus and Visser, 2000).

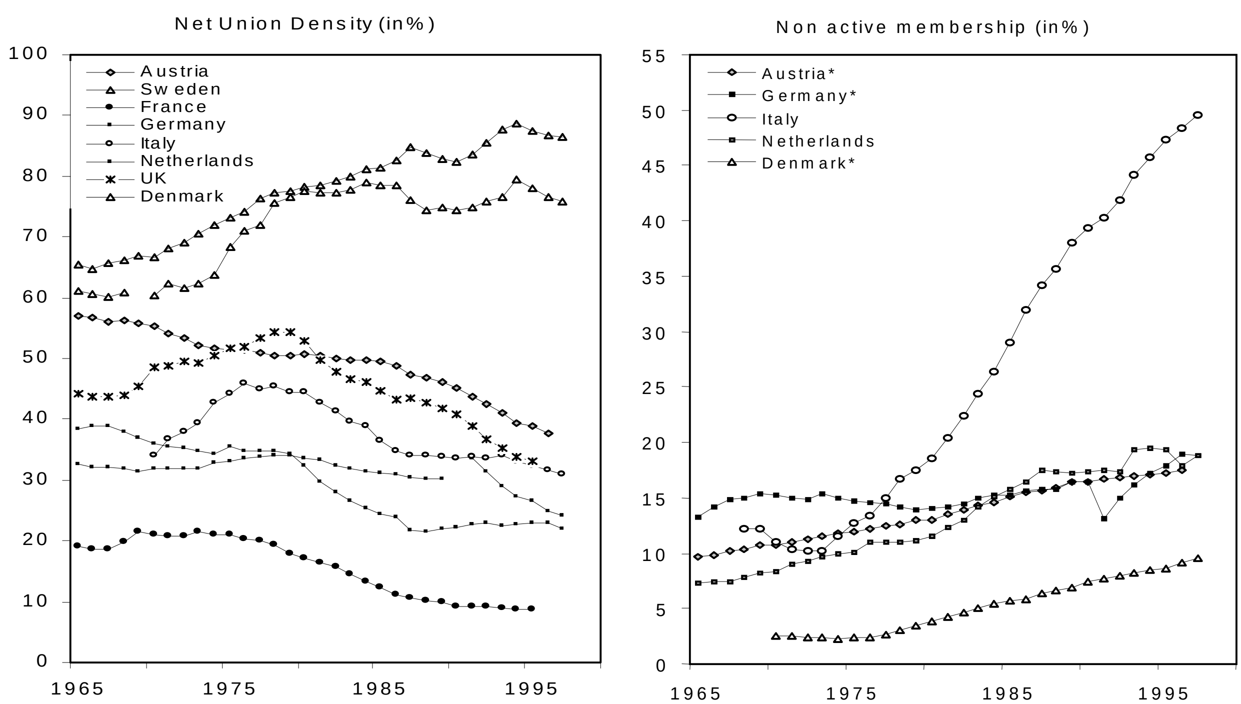
Indeed, it is noteworthy that four Nordic countries – Denmark, Finland, Iceland and Sweden – had the highest unionization rates in the early 1990s. These countries had membership rates exceeding 70 percent, with Sweden ranking top with density over 80 percent. On the other hand, union density in Norway—where unemployment insurance is now compulsory—is only around 55 percent, a remarkable difference to Sweden given the similarities between the two countries in other dimensions. The four countries with the highest membership rates organize their unemployment insurance systems through trade union affiliated funds with voluntary membership. These funds are generously supported by the government. The practice of organizing unemployment insurance through government subsidized but union administered unemployment funds is often referred to as the "Ghent system" after the Belgian town where it was first introduced in 1901. Unemployment insurance in most other OECD countries is based on compulsory rather than voluntary systems. Belgium practices an intermediate system with compulsory unemployment insurance but union involvement in the benefit administration, which provides a similar selective incentive to be member of a union. The large difference between union density in Belgium and the Netherlands can be partly explained by the involvement of unions in Belgian unemployment insurance.

Table 1.3: Union density and non-active members in Western Europe.

	Gross density (%)			Net density (%)			Non-active members (%)		
	1965	1980	1995	1965	1980	1995	1965	1980	1995
Austria	63.0	58.4	47.1	56.9	50.8	38.9	9.7	13.1	17.2 e
Denmark	61.1	80.6	85.5	..	77.5	75.9	..	3.8	8.7 e [~15.0]
France	..	..	..	19.1	17.1	8.6	..	..	[~25.0] x
Germany	37.7	39.1	32.3	32.7	33.6	26.5	13.3	14.0	17.9 e
Italy	32.7	54.5	61.5	28.7	44.4	32.4	12.2	18.5	47.4 r
Netherlands	41.4	36.6	28.4	38.4	32.4	22.9	7.1	11.6	19.3 r
Sweden	..	..	..	65.4	78.2	87.5	[6.4]	[10.9]	[15.3] x
UK	44.2	52.8	32.2	42.6	52.2	32.0	..	..	.. m

Source: Ebbinghaus and Visser, 2000.
Notes: Net density: total members (excluding non-actives) in percent of dependent labour force; non-active members include in some cases students, conscripts and unemployed; e: estimated; r: reported; x: [..] not included in membership figures; m: minimal rate; Italy 1965: 1968; UK net density 1995: Labour Force Survey.

Fig. 1.3: Net union density and non-active membership (in %)



Source: Ebbinghaus and Visser (2000).

While most union movements find it difficult to organize the unemployed and young people, they retain increasingly more and more non-actives, especially pensioners. This trends seems to be certainly true among *Southern* union movements. Unique in Europe is the very high representation of non-actives in Italy, today half of all members are not dependent employed (see Table 1.3).[4] In the other countries, information on pensioners is less readily available as these members remain with their union after retirement and are often not explicitly reported, even if they pay reduced union dues. Across C*ontinental countries*, the rates of non-actives (including some other groups than pensioners) have risen over time. Most European union movements have reached a level between 15 to 25%, still markedly lower than the Italian rate (see Table 1.3), whereas in Britain unions traditionally organise only the gainfully employed. Most frequently, pensioners remain organised in public sector unions, especially railways and civil service grades. For instance in Austria (1994), 40% of members in the railway workers' union, nearly 30% in the postal worker union, and around 20% in the other public sector unions had retired. Union movements have increasing problems to organise the younger workers, thus membership structure ages more and more. But also at workplace level, union shop stewards and works councillors tend to be selected from the core workforce, and are often more experienced senior workers. The membership structure indeed reflects the labour market and social structure of earlier decades, and given the prominence of senior workers within workplace and union decision making structures, union movements face a severe seniority bias.

1.3 Unions as political movement

Union movements have been major advocates for welfare state expansion. They not only used classic pressure group lobbyism, but also links with allied political parties to advance labour and social rights. Early examples were the *British* unions that founded the Trade Union Congress as a platform in order to influence parliament in its labour and social policy legislation as early as the 1860s. They also sponsored the campaign of selected members of parliament, and at the turn of century founded the Labour Party, which they supported and dominated through collective affiliation for most of its existence. In many

[4] Within the three main Italian union movements (CGIL: 55%, CISL: 50%, UIL: 27% non-actives in 1997), the pensioner unions (SPI, FNP, UILP respectively) are at least since the 1980s the largest affiliates.

continental European and Nordic countries, it was the social democratic party that promoted the foundation of a union confederation. Party and unions were two wings within the same socialist labour movement. In *Britain and Scandinavia*, the links between the (blue-collar) unions and the Labour party or Social Democratic party remained institutionalised for most of the post-war period. This certainly brought advantages when the Left was in government but also disadvantages when they were not, most notably under Thatcher’s Conservative government. In recent years, the British Labour Party and the Scandinavian parties have attempted to de-emphasise their formal union links. Especially, New Labour has been reluctant to make campaign promises to union demands before elections, and indeed once in power the Blair government reversed Conservative anti-union legislation only partly, departing from the traditional annullation of the former governments’ acts.

In some *continental countries* religious union movements emerged and maintained links to Christian Democratic parties. However, in France and southern Europe, syndicalist union movements rejected the parliamentary parties and electoral avenue, but were later replaced by union movements that became dominated by communists and maintained close ties to the communist party, while other religious-political movements competed with them for worker allegiance.

These different political legacies still play a role in respect to the fragmentation of labour movements and party-union ties, although there has been some, sometimes significant change. Most notably, the post-war German union confederation (DGB) was founded as a unitary movement, having no more formal ties with the Social Democratic party. The Austrian union confederation (ÖGB) also encompasses different political movements, but allows these to organise in political faction along party lines which maintain close ties with the respective parties. In the Netherlands, the initially very pillarized organisational landscape was remodelled when the socialist and Catholic union movement merged in the 1980s, the new Dutch union confederation (FNV) maintained a more distant relationship to the former political allies (Labour Party and the newly merged Christian Democratic Party).

In all *three continental countries*, union members play an important role in both party families, labour interests have thus a means to influence at least one ruling party at any time. In Austria, the Social Democrats have governed since 1970 alone or in coalition (partly with the Christian Democrats) until 1999, providing the unions close ties to the government. The Kohl government often had to balance within its own coalition the welfare retrenchment position[5] of its liberal coalition partner and the status quo defending social unionist wing within the Christian Democratic Party. Moreover, German pension reforms have been traditionally an interparty compromise, though finding a consensus between incumbent and opposition parties has become more difficult over the last decade. By the same token, the inclusion of union-friendly Left parties may also facilitate blame avoidance. Thus the Dutch Christian Democrats were able to push through unpopular reforms when they brought the Labour Party into a coalition government from 1989 till 1994. But this does not necessarily mean that incumbent parties can easily influence union politics, and indeed governments' efforts towards welfare retrenchment have come under criticism by unions.

In *France*, the Left had been excluded from governing for most of the post-war period until Socialist Mitterand's presidency. The Socialist party has some (informal) support from CFDT (*Confédération Française Democraticque du Travail*), while CGT (*Confédération Générale du Travail*) is closely allied with the Communist Party and the other unions movements are not linked to particular parties. In Italy, the Social Democrats and Socialist had been governing in coalitions with Christian Democrats until 1992, giving the non-communist union movements some influence in government circles, yet the Communist Party and indirectly its ally, the largest union movement (CGIL) remained excluded from power. With the political crisis and realignment of the party system in the 1990s, the three Italian union movements have grown closer together and have concerted with centre-left governments. Party-union ties are not only important in respect to the influence of unions on allied political parties, but also incumbent parties may seek to gain support from its allied unions, for instance, in respect to wage moderation or by not challenging its reform efforts. Yet French Left governments found often only in CFDT a partner for co-operation, while Communist and other unions would take a more hostile approach to reform plans. In Italy, however, the participation of the reformed ex-Communist party (PDS) in the centre-left governments of the 1990s provided a more favourable environment for CGIL's co-operation and paved the way for concentration supported by all three union movements and the government.

In light of the changes in the membership structure outlined above, it is no surprise that unions have lobbied for the interests of current pensioners or those workers close to retirement. In the past, organised labour and allied political parties have mobilised for the

[5] A position in favour of welfare cuts aimed at reducing or stabilizing social expenditure.

expansion of welfare benefits. Especially in countries with social democratic governments that had close ties with the labour movements, most notably in Scandinavia, social security and public services were expanded over the post-war period (Esping-Andersen, 1990). But also Christian Democratic governments, sometimes in coalition with Social Democrats, expanded social transfers, following Christian social teaching and demands by its worker wings (Kersbergen, 1995). But also status division among the workforce has been reflected in union structures. For instance, separate organisations for white-collar workers have been linked to different social rights manipulated by divide-and-rule strategies by employers and the state. Similarly, public employees have been given special pension rights in return for loyalty to the state, and special interest organisations defend today these status differences.

1.4 Unions and social insurance administration

While unemployment insurance are in most countries mandatory state schemes, unions assume in some countries a role in the self-administration of these funds and also labour market administration (see Table 1.6). In Germany, the unions are represented on the tripartite boards of the labour office which is in charge of unemployment insurance and employment services. In Italy, the unemployment schemes are run by the social insurance institute which is governed by a tripartite board. In the Netherlands, the bipartite sector schemes have recently become controlled by a tripartite institute. In France, unemployment insurance has been run by the social partners (thus not by individual unions as under the Ghent system) following a collective agreement in 1958 and largely financed by employer contributions. A particular role is also played by unions in labour market administration in Germany, the Netherlands, Denmark, and most importantly Sweden, where extensive active labour market policies helped reduce unemployment and thus benefited union-run unemployment schemes.

In several countries, the social partners also play a role in the administration of other branches of social insurance. When the first public social insurance system was introduced in Bismarck Germany in the 1880s, self-administration by employers and workers was introduced in return for their joint financial contribution and in order to limit the authority of the central state (Bismarck's initial plans to centralise and finance public benefits by taxes did not succeed). Such self-administration by the social partners was institutionalised in old age insurance in continental European countries, while the Scandinavian and British basic pension schemes were initially only tax financed basic pensions under sole government supervision.

There are also variations among continental European systems (see Table 1.7): they differ in their representativity (tripartite or bipartite, parity or unequal representation) and selection of representatives (social elections or nomination by organisations). Union movements, especially in pluralist union systems, can gain legitimisation by social elections. Even if they have only a low unionisation rate, democratic social elections help them to claim representativity for the entire workforce.

Moreover, representatives receive compensation for their participation in administrative functions, and this can provide an extra source of income for union officials as is the case for the otherwise badly financed French unions. French unionists are heavily financed by the state and social insurance schemes for their participation in self-administrative functions from vocational training to pension schemes. In the words of a French unionists: ‘unions need financial assistance... Only 8% of all French workers and only 6% of those in the private sector pay dues to a trade union. Unions cannot continue to exist and defend employees in the workplace on only 1,000 Franc per year, per member (cit. in EIRO: fr0002138n).’ Thus by receiving reimbursement of expenses, social insurance boards, sickness funds, unemployment schemes at national, regional and local level provide thus many positions for full time union officials. The threat by French employers to withdraw from social security boards in retaliation for the 35-hours-working week legislation has led to major debate over the future of self-administration in France.

Nevertheless, self-administration has not necessarily an impact on policy-making. In many cases the contribution and benefit levels are set by government or parliament. And even when the state had no direct control, governments can increase their influence by providing subsidies and shifting financing towards general taxation. This was the deliberate strategy of the French governments in the 1990s, whether left or right, to increase the general tax for subsidising an increasing share of pension benefits and thus bring the system under state control.

On the other hand, the state may also hold the social partners hostage by shifting costs upon their shoulders. Thus, after German unification, the Kohl government levied some of the social transfers to the East onto the social insurance system which required increases in social contribution and pushed labour costs up. In addition, social insurance contribution already provided solidarity functions, such as credits for child rearing or years of education. The new red-green Schröder government, which came into power in 1998, introduced green taxes to subsidise these social benefits and reduce social insurance contributions accordingly. Still, the principle of parity representation and half-and-half cost sharing, enshrined in post-war German social insurance, has been upheld also with the introduction of a new old age care insurance by the Kohl government in 1995, though on the demand of employers, one former public holiday became a full working day as partial compensation for increasing labour costs at time of increased competition.

Nevertheless, the worker representatives may play an important role in implementation of policies, thus self-administrated schemes particularly at the local level may be able to ignore or even counteract policy changes decided by the central state. In the French system, the supplementary pension system is organised by a plethora of national, regional and local funds run by the social partners and divided by occupational groups. In such a fragmented system, responsibilities are diluted and changes decided at the centre tend to be unevenly implemented. For instance, the Dutch government found it difficult to enforce a tightening of eligibility in disability insurance, given the social partners had misused their supervisory role in the multiple sector insurance boards. In fact, the Dutch government shifted from changing the statutory rules to a redesign of the governance system in order to bring about change (Visser and Hemerijck, 1997). Instead of the paralysed phalanx of post-war corporatist institutions, the left-liberal government introduced a new independent body to supervise and a new tripartite institute to implement changes in the mid-1990s. State intervention in restoring public responsibility in self-administrative governance structure may indeed be a precondition for the effectiveness of welfare reforms in corporatist societies where social partners have used their institutional role for producer coalitions at the expense of the general public.

1.5 Unions and public/private pension mix

Part of the variation in pension spending has to be related to the fact that many countries have in place pension programs which are a mixture of private occupational pensions (typically funded) and public (typically unfunded) social security. In this sense unions may affect both pension policies within the firm or industry and at a national level depending on the Occupational /Public pension mix. In some countries we observe large public programs while in others private arrangements seem to prevail. One approach to document this is to look at the importance of coverage of occupational pensions in different countries. In terms of working population almost all workers in France and the Netherlands are covered due to state extension of collective agreements (nation-wide and sector-wide respectively), while in other countries (Austria and Italy) the fraction of the workforce contributing to these plans is negligible. The number of retirees receiving benefits depends not only on the importance of these schemes but also on their maturity. A similar picture emerges by looking at the funds of occupational pensions which have grown in the late 1990's with respect to the previous decade, though these figures under-represent occupational schemes based on company book reserves (Germany and Japan) and PAYGO-systems[6] (France, German public sector, partly Sweden) (tab.5).

Table 1.4: Occupational pension coverage and funded pension features (late 1990s).

	Pensioners receiving OP	Labour force covered by OP	Dominant benefit	Maturity of scheme	Portability	Indexation
Canada	54% men, 31% women, 41% total	52% men, 36% women, 45% total	Largely DB	Mature	Vesting after 2 years. Little indexation of accrued benefits	Provisions rare; some discretionary increases
Germany	21% men, 9% women	42% total	Largely DB	Immature	Vesting in 10 years. Indexation of accrued benefits	Mandatory
Japan	10% total*	38% total	Largely DB (opt-out of earnings-related state pension)	Immature	Vesting graded between 5 and 30 years for voluntary leavers	Rare
Netherlands	76% men, 23% women, 50% total	90% total	DB around 75% of final salary	Mature	Vesting in one year. Accrued benefits indexed	Almost universal, though not mandatory
UK	66% total	50% total	Largely DB – final salary (opt-out of SERPS)	Mature	Vesting in 2 years. Indexation of accrued benefits	Discretionary, but total or partial indexation quite common
US	47.5 men, 25.5 women, 35.5 total	44% total	Largely DB - final salary	Mature	Vesting in 5 years. No indexation of accrued benefits	Full indexation rare, discretionary increases common

Source: P. Johnson, 1999, Davis (1995) and OECD. DB: Defined Benefit. Funded Schemes are not all OPs. *Figures on recipients in Japan underestimate pensioner rate due to common practice of one-time lump sum benefits.

[6] A Pay-As-You-Go (PAYGO) system of financing is based on a direct transfer of payroll taxes from current workers to finance social security benefits of current retirees, with no accumulation of funds.

Table 1.5. Assets of pension funds as % of GDP in selected countries

Country	**1988**	**1996**
Australia	21.1	31.6
Austria	0.0	1.2
Belgium	2.4	4.1
Canada	26.4	43.0
Denmark	10.9	23.9
Finland	19.7	40.8
France	…	5.6
Germany*	3.4	5.8
Greece	…	12.7
Ireland	29.0	45.0
Italy	…	3.0
Japan*	33.7	41.8
Korea	3.4	3.3
Luxembourg	16.9	19.7
Netherlands	72.7	87.3
Norway	3.9	7.3
Portugal	…	9.9
Spain	0.1	3.8
Sweden	30.9	32.6
Switzerland	64.5	117.1
UK	58.2	74.7
US	36.8	58.2

Source: OECD (1998) Table V.1 * not including book reserves.

Where assets are a large fraction of GDP coverage tends also to be high, implying a prevalent role for occupational pensions. Occupational pensions have assumed a new importance as governments are interested to shift pension provision from public pay-as-you-go systems to private funded schemes. Many wage earners receive today private occupational pensions, which typically supplement rather than substitute public pensions. However, large differences exist as to the coverage, governance, and scope of occupational pensions cross-nationally and also within each country. Occupational pensions may be provided voluntary by employers (Austria, Germany, Italy) or negotiated by the social partners (France, Netherlands, Sweden). In Denmark and the Netherlands, collectively negotiated pensions often are extended *erga omnes* by state decree for all employees within a branch. In Britain, employers are free to decide on such schemes, though they have to follow some state regulation to opt out of the earnings-related state scheme and profit from favourable tax treatment. In those countries, where unions have negotiated occupational pensions, pensions became part of the wage bargaining process. Unions are now confronted with funded schemes even in countries where they had hardly any experience (e.g. Italy). Traditionally, occupational pensions play a very little role in Austria and Italy, while earnings-related public schemes are still of overwhelming importance. Recently, however, Italy has strengthened the second tier of old-age protection by introducing capitalized occupational schemes under sectoral collective agreements. In Germany, the earnings-related social insurance provides for the largest share of retirement income, yet the coverage of occupational schemes is substantial (most non-tenured public employees and half of all private employees) but except for higher white-collar employees it supplements less than 20% of pension income. In Britain, one can opt-out from the public earnings-related scheme, if the private pensions offers equal or better benefits. Currently about two thirds of employees are covered by private or occupational pension plans, the majority is covered by company plans (Bonoli 1999).

In Sweden, coverage by collective occupational schemes is nearly universal through comprehensive collective agreements. They have thus far only supplemented (by 10%) the basic and earnings-related public pension, though their importance will increase in the future. In France, occupational pensions were made mandatory by state legislation in 1972, thus coverage is virtually universal. Since public pensions typically provide not more than 50% of final pay, the occupational pensions make a significant contribution to maintaining the standard of living, especially for higher earning employees. In the Dutch pension system, the occupational pensions are nearly as common thanks to collective agreements and they contribute to a sizeable share of income during old-age, since the public scheme provides only a universal flat-rate benefit regardless of previous employment.

A distinction emerges between countries which have adopted a *Bismarckian* approach in their pension provision, and have earnings related public pensions with relatively high replacement rates such as Germany, while Anglo-Saxon countries tend to follow more a *Beveridgean* pattern and possess a more substantial “second-tier” where the first tier is more modest. Tables 1.4 and 1.5 also show that almost all of these countries have mainly adopted DB plans, vesting rules are very strict in Germany and less so in other countries, on the other hand tight vesting rules are often associated with reasonable inflation protection for the beneficiaries. Recent evidence (Andrietti, 2000), suggests however that there is a distinctive move in Europe toward the emergence of DC schemes.

Unions are typically involved in private occupational insurance. Traditionally they have provided social insurance as part of mutual self-help traditions. In France, the first supplementary insurance was introduced by the organisations for managerial and professional staff (‘cardres’) in 1947, a collective agreement for other workers was signed in 1961, and supplementary pension was made mandatory in 1972. Two federations, for cadres and for employees, co-ordinate the many occupational, regional and local funds that exist and are governed by bipartite boards with employer and union representatives. In Sweden, four major supplementary occupational pension schemes have been established by collective agreements. They are run by the unions in the blue-collar, white-collar, central state and local state sectors and the respective employer (associations).

In the Netherlands, occupational supplementary pension schemes are sometimes run by larger companies, but also several sector-wide bipartite schemes were established by collective agreements. In addition, sector-wide schemes for early retirement bridging pensions were negotiated by the Dutch social partners in both private and public sectors. Also Denmark has a mixture of partly negotiated and partly individual pension schemes, while in Germany only public employees (other than tenured civil servants) have a negotiated occupational pension scheme. In Denmark, France and the Netherlands, the social partners have used their supplementary pension, unemployment or special ***preretirement*** funds to allow widespread practice of early exit form work , thereby filling the replacement gap of (or lack of) public early retirement benefits.

In the voluntary occupational pension schemes that are widespread in Britain, pension funds are sponsored by the employer. The employer nominates the trustees, while the workers have usually no representation rights, though their company pension (and more recently also personal insurance) allows them to opt out of state supplementary pension. Many larger German private employers also provide voluntary occupational pension (via book reserves, insurance plans or pension funds), yet works council and workers have only limited say. The British and German occupational schemes, at least those that provide defined benefits have been used in the past to co-finance early retirement in the case of restructuring or closure.

In recent years, in Austria, Italy and France, funded occupational pensions were promoted as an safeguard against the demographic problems with publicly mandated pay-as-you-go systems. In Italy, the social partners were able to negotiate occupational pensions in some branches, partly integrating the end-of-service pay, a deferred wage under many past collective agreements. In Austria, tax exemption are only granted for non-negotiated voluntary employer contribution (that is fringe benefits, not deferred wages), which has limited the growth potential for negotiated occupational schemes. In France, the Conservatives plans for promoting funded private pensions, has been halted by the government change to the Left. The Jospin government seems more keen to extend the reserve funds for the current systems, then to foster pension funds *à l'anglaise*.

The structure of the public/private mix might shape the incentive structure of unions in two ways. First, the public—private mix is important for understanding the role and strategy of unions. In mixed systems, employers and unions play a larger role in welfare provision, they sometimes fill the gap left by public policy. Thus, cuts in public welfare benefits, for example, might be compensated by improvements in collectively negotiated occupational schemes. However, the larger the private share, the more welfare costs are internalised by employers and employees. This might induce a greater cost awareness of pension spending on the side of the unions, while in public schemes, unions could press for a higher state subsidy instead of welfare cuts.

Rent seeking is most pronounced in pension arrangements which cover only a small segment of employees but which are financed out of general taxation. For instance, German civil servants pensions are not financed by contributions but by the public budget, and thus they may have lower incentives to accept benefit cuts than employees with social insurance who have to pay higher contributions with increasing beneficiaries. In particular, a high financing share of the state (or of the employers) is likely to moderate the goal conflict between the interests of wage earners and pensioners within the trade union.

1. 6 Institutional and Political Veto Points

In addition to the political influence as lobbyist, unions have often an institutionalised role in the social policy decision-making (see Table 1.7). The legislator and governments consult with unions informally or in some countries consultation of the social partners (unions and employer associations) is formally institutionalised. Like in EU social policy making, where the European Economic and Social Committee has to be formally consulted, several continental European countries have statutory tripartite councils for social policy consultation, sometimes dating back to state corporatist legacies. Given the relative heterogeneous and indirect interest representation by these corporatist institutions, the impact on law making and shaping policy making is rather limited, though it may shape public debates by voicing the plurality of interests at stake. France' very heterogeneous and divided Economic and Social Council (CES, since 1947) has the broadest statutory consultation role, but has often been instrumentalised (or just ignored) by governments. The Dutch Social-Economic Council (SER, since 1950) has been influential in the heydays of corporatist consultation but its more recent reform proposals have been several times overturned by the government. The Italian National Labour Council plays a rather secondary consultation role.

The Austrian Chambers (labour, commerce and industry, agriculture) are formally part of social policy making (and collective bargaining). The representatives to these statutory Chambers are elected at regional level (membership in the Chamber of Commerce and Industry is compulsory for firms, and in the Labour Chamber, the different political currents stand for election). Since labour, capital and agricultural interests are represented separately, approval by all Chambers requires informal compromises struck by the main associations.

Such formal consultation have not been introduced in Germany nor Scandinavia, though informal consultation with the social partners does take place and reform commissions include traditionally organisational representatives besides experts. In the UK, policy proposals have often been developed by partisan policy institutes, and royal commissions may include individuals connected to particular interest groups. However, the British government has probably the largest leeway in formulating policy proposals.

Unilateral welfare retrenchment by governments may provoke collective action, ranging from one day mass demonstrations as in the Netherlands in 1991 to month long mass strikes as in France in 1995. Despite declining density rates, union movements are still the largest collective mass organisations in modern industrial societies, and thus the rather unusual mobilisation of their membership to protest government policy sends a major political signal. When in the summer of 1991, the Dutch left-centre government announced major welfare cuts, the unions called out for the largest post-war demonstration (one million people) in the streets of the capital (Visser and Hemerijck, 1997: 117). This struggle also divided the Labour party but Kok as party chairman was able to win the majority vote for the government plan at a special party congress. Yet the next election in 1994 brought major losses in votes for both, the Social Democrats and Christian Democrats. Mass demonstration have largely a discursive and symbolic function, they voice protest in the public debate and indicate that more severe political consequences may follow from unilateral state action. Since union movements are still mass organisations, politicians may worry about electoral consequences, though much depends on the rules of the electoral system and the majority position of the government at the time. Moreover, unions may counteract in the collective bargaining realm what they have lost by changes in the law. A good example is the unsuccessful attempt of Germany's government to change sick pay by legislative means (Schludi 1997).

A more severe threat than demonstrations maybe strike action against the government. The French strike wave in the winter of 1995 that followed the retrenchment plans by the Conservative government under Juppé is a case in point. Especially the efforts to cut the special pension schemes in the public sector (in line with unopposed cuts in the private sector that were introduced by the Balladur government in 1993), led to massive spontaneous strike by public sector workers that later were supported by their unions and the general public. The government, after ad hoc consultation with the unions, back tracked, postponing the major cuts in the public sector pension schemes. Already a year earlier, major demonstrations and strikes against retrenchment efforts by the Berlusconi government were successful in bringing down the Conservative government and leading to concertation with the new centre-left Dini government on a consensual welfare reform.

Under Britain's Westminster political system and centralised social security system, the possibilities for unilateral government action are most uninhibited. Moreover, the strategy of the Conservative Thatcher government to 'take the unions on' in the industrial relations realm by removing past union immunities, regulating strike ballots, and abolishing closed shops successfully weakened the unions. Moreover, the symbolic victory over the miner strike in 1985/86 provided a further indication how weak British unions were when facing a government determined to privatise public services. Nevertheless, welfare retrenchment in popular public programmes, especially the National Health Service, remained more limited and gradual (Pierson, 1994).

Moreover, collective wage bargaining has also an impact on welfare state expenditures. Unions have been in favour of linking pension benefits of public pay-as-you-go systems not merely to inflation but also to wage gains, thus senior workers and current pensioners are assured that pension benefits keep up with rising living standards. Thus, their wage bargaining policy has consequences for welfare expenditures by the linkage between wages and social benefits (Hassel and Ebbinghaus, 2000). In addition, public sector wages determine an important part of the public payroll and thus public expenditure, not to speak of the problems of a spill over of excessive wage increases into the private sector. In countries where retired civil servants are not covered by social insurance but receive retirement pay from the public purse (as in France and Germany), public wages determine not only civil servant wages but also pension levels. Moreover, these often favourable conditions have reinforced status divisions between civil servants and other public and private employees as well as led to a high degree of organisation which in turn defend their special status. Thus cuts in the pension system for the private sector may not be carried out in the public sector.

Table 1.6: Governance in Unemployment Insurance and Labour Market Administration.

	Unemployment insurance	**Labour market administration**
Austria	mandatory unemployment insurance (1920) under Ministry of Social Administration, employer and employee contributions, state subsidies for assistance	local and regional labour offices under Ministry of Social Administration
Denmark	voluntary union-run unemployment funds (Ghent system, since 1933 state subsidies), supervised by Ministry of Labour	Employment exchange run by local unemployment fund
France	voluntary unemployment scheme (UNEDIC) run by social partners (since 1958 collective agreement)	ANPE (1967-), national public agency with local offices, administered by Labour Ministry
Italy	separate schemes, including industrial redundancy scheme (CIG), administered by INPS (tripartite board)	local and regional offices of labour
Netherlands	WW (1952-) short-term unemployment insurance: bipartite industrial insurance boards controlled by tripartite Social Insurance Council, since 1995: LISV (tripartite board) WWV (1965-)+RWW long-term unemployment and social assistance: local government, controlled by Social Ministry	since 1991 tripartite Employment Boards (replaces 1930 labour exchanges)
Germany	mandatory public insurance scheme (1928-) run by Federal Labour Office (tripartite administration), employer and employee contributions plus state subsidy	local and regional branches of Federal Labour Office (tripartite administration), state subsidy
Sweden	voluntary union-run unemployment funds (Ghent system, since 1934 state subsidies), supervised by AMS since 1974 unemployment assistance for uninsured by county labour market board	local employment service, supervised by National Labour Market Board (AMS, since 1949, tripartite)
UK	National Insurance Fund (job seekers allowance), administered by ministry	employment offices under Department of Employment administration

Source: Flora, 1986, Appendix volume; MISSOC, database.

Table 1.7: Governance in Social Policy-Making, Public Pension Schemes, and Private Occupational Pensions

	Corporatist policy making	Self-administration in pension scheme	Collective / private occupational schemes
Austria	Statutory Chamber of Labour (elected worker representatives), statutory consultation in policy-making	Tripartite self-administration of seven occupational pension funds +	recently: supplementary private pensions
Denmark	None (occasionally: tripartite Royal Commissions)	none (public pension scheme supervised by ministry: basic pension administered locally, supplementary pension centrally)	Collectively negotiated and private occupational pension schemes; collective negotiated early retirement pay (efterløn)
France	Statutory Social and Economic Council (worker, employer and general interest representatives), statutory consultation in policy- making	national, regional, and local funds governed by state nominated director, but bipartite board (social elections) *	Supplementary pensions set-up by collective agreements (1947- cardres, 1961- other employees, made compulsory in 1972), two federations of various local funds governed by bipartite boards
Italy	Statutory National Labour Council, consultation role	public National Institute (tripartite board nominated by organizations) +	since 1990s: collectively negotiated sectoral pension funds
Netherlands	Statutory Social-Economic Council (tripartite), consultation in policy-making; voluntary bipartite Labour Foundation makes policy recommendations	public pension scheme (bipartite self-administration by Labour Councils, supervised by Social Insurance Council; since 1995: tripartite central supervision)	sector wide occupational schemes (bipartite, sometimes erga omnes extension); also sector-wide early retirement schemes (VUT, bipartite).
Germany	None (Sozialbeirat advisory to ministry)	bipartite self-administration of regional blue-collar or central white-collar schemes (social elections) +	in private sector: voluntary occupational pensions by employers, in public sector: collectively negotiated scheme for non-tenured public employees
Sweden	None (occasional tripartite Royal commissions)	none (public pension scheme supervised by ministry)	Collective negotiated four (two private, two public sector) major occupational pensions (bipartite)
UK	None (Royal commissions may include union representatives)	none (public basic and supplementary pension schemes supervised by ministry)	Voluntary private pension trusts sponsored by firm (rarely worker representatives on board), opt-out option of state supplementary pension

Sources: Ebbinghaus and Hassel, 2000; Flora, 1986, Appendix volume; EIRR, : passim; EIRO, : passim; MISSOC, database.
+ contribution and benefits are set by legislator; * French employers threatened to withdraw from social administration in retaliation to 35hrs law

2. Unions and Pensions: Theory and Policy Implications

In our introduction we have highlighted some stylized facts on the typical union activities:

(1) they carry out wage bargaining and rent sharing activities in non (perfectly) competitive product markets;

(2) they express "voice" at the workplace and directly (or indirectly) provide social services and social protection to union members.

We have looked at bargaining and rent sharing and social services (insurance) provision activities in relation to different welfare systems. There are obvious interactions between the public social insurance systems and the unions' activities. There are also important interactions between the two roles sketched above: the provision of social services and the protection against negative outcomes may directly or indirectly affect wage bargaining, in some cases unions will make use of a "broad" bargaining agenda including current wages and pensions – for example.

The policy questions are then:

- Is the action of unions as "service/insurance providers" efficient?
- If there are some gains – e.g. the role of unions is welfare improving for union members and possibly for all workers – are there some costs to be paid by workers, firms or society at large?
- How effective and efficient are union efforts to redistribute income toward members and low income groups of society?
- Can union play a political role in "long term commitments" that substitute for government short spanning of policies?

2.1 Basic Economic Theory

In this section, we sketch a simple analytical framework, which is useful to organize our thinking on the impact of trade unions on non-wage benefits and their relation to wage and employment issues. The presentation is kept at a minimum technical level. A more formal analysis is provided in the Appendix.

The most intuitive connection between old age pension contracts and activities of unions can be seen in the framework of pension funds. In 1 we have documented the importance of pension funds in the form of occupational pensions in the pension system of many countries and the variation in the public/private pension mix across countries. Occupational pensions are typically collective insurance schemes for old age offered by employers to employees within a firm or an industry. It is still debated whether it is best for a worker to insure through a pension fund or to insure individually with an insurance company or through individual contracts (a personal pension like in the UK). It is often claimed that pension funds are superior in that there are economies of scale, the loading factors on the insurance contract are mitigated due to both the collective nature of the contract and the young age of the insured population and, finally, because in many cases the employer's contribution would be lost when moving to an individually purchased annuity. The main argument against group-insurance is portability of pension rights, as the back-loaded[7] nature of benefits accruing in pension funds (often of a defined benefit form) provide an advantage for those who stay at the expenses of more mobile workers.

In this context pensions can be regarded as deferred wage and therefore they are part of the employment contract. I.e. there will be a "broad" bargaining agenda set by unions. The idea that pensions are fringe benefits and therefore unions bargain over pensions goes back to Freeman (1981). Workers who are more attached to the firm also have more weight within the union. These tend to be older (more senior) workers as younger workers tend to be more mobile. Because unions represent the median voter (i.e. the typical worker also referred to as the infra-marginal worker) they tend to push for fringe benefits (particularly higher pensions) reflecting preferences of older workers. It emerges that unionized firms offer fringe benefits to older workers as a substantial part of the full spectrum of union seniority advantages. In particular they offer participation to pension funds. Pension funds of a DB form have prevailed in the UK, in the US and also in the NL. These contracts exacerbate the seniority aspect as not only pensions are fringe benefits earmarked for older workers, but DB benefits are higher for workers who are loyal to the firm – stayers - (and therefore to that union).

[7] Occupational pensions often have a back-loaded nature in the sense that the value of the pension rights that workers accrue tend to increase with seniority and there is a redistribution within the fund from mobile workers to more stable workers.

If one thinks of pensions as deferred wage, this involves a broad bargaining agenda with a particular twist: the inter-temporal nature of the contract becomes relevant. In particular there is a risk associated with the long run occupational pension benefit (OP) which does not affect current wages and may not affect other fringe benefits. For example the worker may be detached from the firm (Askildsen and Ireland –1997) and a leaver may be unable to claim for the OP-benefit from the original firm or he may receive an OP benefit much lower than a stayer, other things being equal . In this framework the role of unions rests in their ability to manage three variables: current wage, OP benefits and employment in the presence of potential trade-offs. ***There exists a potential role of commitment by unions on the delivery of long term benefits*** (by the firm) when the firm cannot guarantee a credible commitment. However informational problems may also give rise to the possibility of collusive behaviour between firms and unions at the expenses of workers.

The interaction of unions and government pensions is also complex. The behaviour of unions in different countries seems to reflect some basic patterns. Unions seem to favour public pensions vis-a-vis private arrangements, and when private arrangements are in place (occupational pensions) they seem to favour DB plans rather than DC plans. In general unions tend to preserve the status quo when it comes to retrenchment on pension policies (see Section 4).

2.1.1 Model 1. The basic framework with Homogeneous Work Force.

There are three basic elements to take account of in this context: (1) the bargaining framework (2) the economic variables that unions can affect and (3) the institutional setting (the actors). The combination of these features can give rise to a variety of results. We can anticipate up-front that one major result of this theoretical exercise is the impact of employment protection policies, often taking the form of "soft landing plans" on the effects that the action of unions can exert on wages, employment and other benefits.

The actors and the (simplifying) assumptions

Workers are concerned with both their current wage and their future income in the retirement period. This has two components: an "occupational pension" and a public old age benefit. While occupational pensions are completely determined by the employment lifetime status, public provided old age benefits represent a safety net in that they are not related to previous labour market conditions. While occupational pensions are part of the employment package – public pensions are financed through a payroll tax levied on workers. As a first approximation we do not consider the government budget constraint.

There is a pool of workers: employed workers, receiving a wage and the (fulfilled) promise of an occupational pension, and unemployed workers. Workers have no access to credit/insurance markets while the firm has perfect access to these markets.

Following Freeman and Medoff (1984), and Askildsen and Ireland (1997), we assume that an essential feature of a typical worker, distinguishing the short run from the long run, is the fact that workers are more subject to some basic uncertainty in the long run than in the short run. For example a worker faces some uncertainty about his future attachment to the firm in the second period of his life. Initially we assume that this basic uncertainty is determined by some external condition and it is not related to the individual or to the firm. An unemployed worker receives an unemployment benefit while young but he does not receive any occupational benefit when old - he simply enjoys the transfer emanating from the public benefit system.

The literature discusses on the appropriate objective function of the union and the bargaining game played between unions and firms (see Oswald 1982). The standard situation, in the trade union literature, is a monopoly trade union with "right to manage". Hence at a first pass, we take the standard view that, given a pool of workers, the union wants to maximize the welfare of the representative member who may be employed or unemployed with given probabilities. We consider that the firm sells a product, which generates a revenue function in the present period, this is increasing in the employment level. The firms wants to keep a given level of profits in order to be part of the relationship with the union and the optimal employment level is ultimately the result of the firm's decisions process.

Monopoly trade union

The union will face the typical trade-off between the level of wages and occupational pensions (OP) paid to employed members and the probability of employment for its representative worker. Furthermore, there are two dimensions of the problem: the trade off between "total cost of hiring (current wage plus present expected value of future OP)"[8] and employment and also between current wages and future occupational pensions. First, the theory provides an optimal trade off between wages and occupational pensions from this basic set up for a given "total cost of hiring". Then the problem of deciding employment collapses to the fairly standard problem of the monopoly trade union.

It is interesting to see how, in the simple framework sketched above, wages, occupational pensions and employment change with variations in the probability of attachment to the firm (or concern for long term benefits), the level of unemployment benefits (UB), the level of public pensions and payroll tax rates.

For example, an increase in public benefits, for a given cost of hiring, will move the tradeoff between current wages and deferred benefits in favor of current wages, as public benefits partially substitute for occupational benefits. Occupational benefits are partly crowded out by public transfers but by less than one for one, so total long term benefits increase. However if one looks at the overall impact than an increase in public pensions increases the union's incentive to choose a high total labour cost with an associated lower equilibrium level of employment. The intuition is the fact that, as public transfers are not conditional on employment status, they tend to reduce the value of employment relative to unemployment for a trade union member while working. This, in turn, makes the trade union more willing to ask for higher total labour costs and lower employment. As a consequence, equilibrium current wages will also increase with public old age benefits. In general, total pensions are also likely to increase. Occupational pensions are partially crowded out by public pensions, at the same time, there is an additional income effect coming from the fact that the equilibrium intertemporal labour cost increases. The whole effect of public pensions on occupational pensions is therefore on a priori grounds ambiguous. When the (positive) impact of public pensions on wages and labour costs is strong enough, there is a complementarity between public pensions and occupational pensions, so they grow together.

The impact of the probability receiving an occupational pension is a bit less straightforward. Various effects are at work. First, as the likelihood of receiving future benefits increase, workers tend to value more these benefits relative to current wages At the

[8] We refer to this expected lifetime compensation (from the point of view of the worker) or total

same time however, a higher probability increases the effective price of occupational benefits relative to current wages for the firm. This, in general, will induce traditional "substitution" and "income" effects on wages and occupational benefits. The substitution effect tends to increase wages and reduce benefits, the income effect tends to reduce both. Generally, one may conclude that the total effect of an increase in the “survival” probability is to reduce current wages and occupational benefits. There are also indirect effects to consider. A higher value of the attachment probability increases the worker's value to be employed today by the firm as it increases the probability to receive in the next period occupational benefits, which are employment status dependent. This implies that the union will be relatively more concerned by employment than by labour costs, reducing therefore the union's incentives to demand high labour costs. As a result, the equilibrium expected cost of labour is lower and the employment level higher. Given that the direct impact of the probability on current wages and occupational benefits is negative, this implies that the total impact of an increase in the “attachment probability” (directly and indirectly through the induced effect on wages) is to reduce equilibrium current wages and occupational benefits.

Finally, let us close this by investigating the effect of an increase in the payroll tax rate. In this framework one gets the standard result (Alesina and Perotti, 1998) that the union passes to the employer some fraction of the fiscal burden and that the union equilibrium labour cost is increasing with the tax rate. An increase in the payroll tax, everything else being equal, has therefore a negative impact on employment. The effect on current wages is generally ambiguous. The direct impact of an increase in the tax rate is negative but there is an additional positive income effect via wages. For occupational pensions, it is quite likely that in general they are also increasing in the payroll tax.

Bargaining

The simple model of the previous can be extended along several dimensions. First one may generalize the analysis to situations where the union bargains with the firm on wages and benefits, while the firm keeps its "right to manage" on employment decisions. Results are qualitatively the same as in the monopoly model of trade union.

labour cost or total cost of hiring (from the point of view of the firm) as “total compensation”.

One can also consider the situation of full bargaining between the firm and the union on the three dimensions current wages, occupational pensions and employment. The main difference with the previous case is simply that now there are a set of optimal contracts in wages and employment governing the relationship between the union and the firm with an outcome implying more employment than in the "right to manage" case. The smaller the bargaining power of the union, the lower the labour costs, current wages and deferred benefits. Again, one will get the same qualitative results as in the case of the monopoly union model for simple comparative static.

2.1.2 Model 2. Political economy considerations within the Union. Workers differ by age-seniority.

So far we considered a framework in which all workers were identical. Obviously, one of the important features of non-wage and benefits policies for unions is the fact that they do not affect all workers the same way. In this , we discuss the impact of some heterogeneity across workers' preferences with respect to long term benefits and employment. Various dimensions may be captured by such differentiation: age, seniority or degree of attachment to the firm. As long as unions can be viewed as groups taking collective decisions along more or less democratic rules, this introduces a number of interesting political economy issues within the union. *What are the points of conflicts or convergence between young and old workers inside the union?. Which kind of preferences of the various workers are represented in the objective function of the union? What is the effect of workers heterogeneity on wages, pensions, employment, membership?*

Young workers may work in the first period of their life and retire in the second period (if still alive). Old workers, in predetermined fixed number, are retirees and live only in the first period. They do not work and receive benefits in that period. At the beginning, the "monopoly" union chooses the current wage rate of young workers and their future occupational benefits to be paid at retirement. Given this, the firm chooses the employment level. In the last period, benefits are paid to workers previously employed.

We will first assume that the structure of political representation within the union is such that the union's objective function will take account of young workers, given some veto power of the old workers to receive what they were promised (i.e. their occupational pension benefits). The problem of the union is basically the same as in the previous except for the fact that now the firm has to generate a large enough surplus to make sure that benefits to current old workers can be paid out.

The equilibrium labour cost of young workers is then, at least in some range, a decreasing function of the size of old workers in the union. A larger current surplus and a lower associated labour cost is necessary to accommodate higher expenditures of the firm on occupational pensions of old workers. From this, employment of young workers is positively related to the size of old workers in the union. The intuition is simple. A larger volume of occupational pensions paid to old workers induces the union to moderate its demand on labour costs for the next generation of workers in order to generate a high enough firm's surplus, and in turn it generates high employment. Still, it should be noted that such a situation is not in the interest of the young workers. Indeed, the welfare of a young trade union member is decreasing with the size of old workers in the union.

Obviously, this aspect has interesting implications for the dynamics of membership inside the union. Consider for instance now that trade union membership is endogenous and that young workers do enter in the union when their expected welfare in the union is large enough. The preceding discussion implies that young workers will be less likely to enter the union, the larger the size of retired old workers.

From this, it follows that aging unions with larger size of retirees on occupational pensions should have more difficulties attracting young workers and that their membership should decline overtime.

Voting on benefits and wages

In the preceding framework, the decision making process within the union on current wages and occupational pensions was quite simple. The objective function of the union represented the preferences of the young workers under the constraint of veto power of the old retiree members who did not work. One may reasonably think, though, that the political game within the union can take some other forms with, obviously, different implications for current wages, pensions and benefits. In particular rather than having only workers and retirees, one may think that there are also middle-aged workers who have intermediate preferences over wages and benefits and whose position might be pivotal for the representation of the union's objectives in the bargaining game with employers.

A simple way to investigate such issues in our framework is to follow Askildsen and Ireland (1997) and assume that workers inside the union now are continuously differentiated according to their relative attachment to the firm (survival probability in the firm or seniority). A worker characterized by a given attachment level will, as before, take into account the probability and the contingency of unemployment in taking decisions. The difference is now the fact that, if employed, that worker will expect to receive occupational benefits differentially (i.e. according to his attachment). On the other hand, from the point of view of the firm, the unit labour cost to hire a worker will be the sum of the current wage and the expected cost of paying an occupational benefit. As we have now some degree of heterogeneity across workers, one needs to take into account the political mechanism by which collective decisions will be taken within the union. Let us consider first the case where wages and benefits are decided by simple majority voting. Each union member will have a preferred policy outcome which will depend on his attachment probability, the average attachment probability in the union and the various parameters of the problem.

When a voting equilibrium inside the union exists, the equilibrium choice of labour cost, current wages and deferred benefits, will be the one preferred by the trade union member with the median characteristic, from which we deduce the equilibrium employment level. Hence changes, within the union, in the distribution of attachment probabilities, affect the equilibrium values of current wages, benefits and employment.

Consider first that on average unions' members are more attached to the firm. For a given employed worker, an “exogenous” increase in average attachment increases the "price" of occupational benefits paid by the firm. The value of being employed for any trade union member is consequently reduced. This leads in particular the median member (or pivotal agent) to prefer a higher expected cost of labour and a lower employment. Holding the median member constant, the impact on occupational benefits is unambiguously negative, for occupational benefits are now, ceteris paribus, more costly to the firm. The effect on current wages is a priori ambiguous but is likely to be positive if the income effect through the wage is large enough.

Consider now an increase in the attachment probability of the pivotal agent. This may be interpreted as the fact that people more concerned or attached to the firm get more political power within the union. In that case, obviously the pivotal agent in the union wants higher long term benefits. At the same time, because occupational benefits are attached to employment, the pivotal agent also cares more about employment. Consequently, his preferred level of total labour costs (current wage and future occupational benefits as a package) is reduced, current wages are reduced and employment is increased.

2.2 What Unions Do in Practice: analytical considerations

The simple model sketched above has two main messages. (1) There are a number of economic variables which may be affected by the action of unions at the same time, particularly wages, employment and occupational benefits. Depending on the bargaining setting and the macroeconomic framework (generosity of public pensions and unemployment) we may observe different results.(2) Institutional details of the relationship between the union and the firm will matter for the determination of current wages and deferred benefits. Full bargaining on wages, benefits and employment implies lower unemployment than the "right to manage" case. Current wages and occupational benefits are an increasing function of the strength of the union.

Hence one may conclude that***:***

- *Stronger unions should lead to an economic set up characterized by low unemployment high current wage and a high occupational pensions.*
- *Public pensions, partly or entirely substituting for Occupational Pensions also are associated to an optimal trade-trade off between employment and wages.*
- *Also, to the extent that the PAYG constraint is not internalized by unions (e.g. in case of decentralized bargaining) high pensions should be associated to higher unemployment and higher current wages. If, on the other hand, the PAYG constraint is internalized then large pension programmes exacerbate the trade-off between wage demand and*

employment and one would expect less generous pension provisions in a centralized setting

However this simple model can be extended to allow for a number of important features which we observe in reality.

2.2.1 Insiders, last-in-first- out rules and soft landing plans.

An important aspect of the theoretical analysis is whether members of the union face all the same probability of being unemployed. In reality, this actually does not hold. Some workers within the union may typically enjoy insider positions within the firm and therefore may face very little risk to be fired under bad external conditions. Also, very often, firms and unions subscribe to seniority rules and last-in-first-out (LIFO) conventions. These mechanisms discriminate between young workers and more senior workers in terms of their risks to be unemployed and their access to occupational benefits. Another dimension of implicit employment discrimination across workers is the use of "soft landing" plans like early retirement plans, long term unemployment insurance and disability plans to mitigate unemployment problems. As these plans are mainly applied to senior and older workers, they induce a differential outside payoff according to age or attachment in case of unemployment. More attached or older workers are also more likely to be insiders and their employment status is less sensitive to wages than that of junior (mobile) workers. In a full bargaining model with voting, this in turn affects differentially the preferred labour package that the worker would like to vote for in the union.

It follows that more senior union members have higher probability to be employed and therefore value more an increase in total lifetime compensation than without such rules. Since their probability of employment is less sensitive to total employment cost, they are also less concerned about the impact of an increase of the labour cost on their change of employment status. Also, because of the possibility of "soft landing" plans, their reservation payoff level in the contingency of unemployment is increased, inducing them to demand more on the labour cost.

The implication of this generalization is striking and has to be contrasted with what was obtained in the absence of seniority rules, FILO-conventions and "soft landing" plans.

As the pivotal agent (representative agent) in the union becomes more attached to the firm, he also gets more protection against the risk of unemployment through seniority rules, FILO-conventions and ''soft landing'' plans. Hence, his preferred labour cost increases and the employment level decreases with respect to the standard case. Current wages and occupational benefits are now both increased.. The cost of such a strategy is paid by junior workers who have a disproportionately high probability of unemployment. Hence stronger (older) unions in this case will be associated to an economy with high youth-unemployment, high current wage and high occupational benefit.

2.2.2 Concern for membership

We have argued that the internal age structure of unions is important and we have documented important changes in membership. Suppose now that membership is endogenous. Workers are indexed by the characteristic (survival in the firm) and decide to join the union by comparing their expected payoff inside the union to the welfare they might get in some other occupation in the non-unionized sector of the economy. Clearly, in order to decide to join the union, each worker has to anticipate what will be the political equilibrium inside the union. This depends obviously on the position of the pivotal agent within the union who in turn is determined by the type of individuals who decide to join the union (Booth-(1984)). Hence an equilibrium with endogenous membership should determine jointly the political equilibrium decided within the union, the size of the union and the nature of the pivotal agent within the union.

When seniority rules, LIFO-conventions and "soft landing" plans are applied within the union, then the union reflects the political interest of workers with a high attachment or seniority characteristic, and the less it is interesting for a mobile or young worker with a low attachment probability to join that union. Therefore only workers who expect to have long-lasting relationship with the firm tend to become members of the union. At the same time however, the position of the median member of the union is itself endogenous and dependent on the characteristics of the individuals who decide to join the union. The trade union will be, on average, composed more of workers having high concern for future benefits and seniority.

This two-way complementarity between the attachment of the median worker and the characteristics of the potential union member implies that there may be ***multiple equilibria in union membership, wages and benefits***. The intuition for such a possibility is quite simple. When the union is mainly composed of workers with a low attachment probability, the political equilibrium within the union is more likely to reflect the preferences of these workers with high employment, relatively low wages and low benefits. Anticipating this, more workers of these types will join the union in the first place. At the same time however, one may have another equilibrium in which the union is mainly composed of senior workers with high values of the attachment probability and protected from unemployment by seniority and LIFO rules. The political pivotal worker within the union is, in this case, more likely to reflect the preferences of these workers with high wages and benefits, at the cost of a high probability of unemployment for junior workers. This in turn obviously discourages union membership of the latter and supports a structure of union membership biased towards senior workers.

One way out is to think of a long term perspective. We have to allow for the possibility for mobile or young workers to become eventually senior or insider over time. Taking into account such possibility reduces the potential opposition between young workers and more senior ones. More precisely, extend our framework and consider that, in the second period of their life, workers can share their time between work and retirement. Because of this, junior workers now anticipate that they might become senior in the firm and enjoy the associated social protection and benefits.

2.2.3 Representative democracy, lobbying and gerontocracy

In a direct voting mechanism - where implicitly workers had equal voting weights - the results reflect the preferred outcome of the median or pivotal agent of the union. As in any other relatively large social group taking collective decisions under democratic rule, one may think, however, that public choices decisions inside the union are more likely to be taken by some kind of representative democracy. This entails two new features. First, one may expect that the interests of particular groups of workers will be over-represented while, on the contrary, other groups will be under-represented. Groups which are more effective at lobbying inside the union will be more successful at pushing their preferred outcome on the union agenda. Second, the union's representatives may have different concerns than the median or the pivotal agent in the union. Therefore the true objective function of the union might be quite different than the one described until now.

Concerning the issue of over representation and lobbying, one may expect the general argument of Salai-i Martin and Mulligan (1999) on gerontocracy and comparative advantage at lobbying of old and senior people to work especially well at the level of trade unions. The argument rests on three elements. First, the technology of lobbying or political influence is time intensive rather than money intensive. Second, senior workers and retirees have a lower opportunity cost of time than junior and active workers. Finally there a crucial asymmetry in the sense that old and senior workers cannot be young or junior anymore while, on the contrary, young and junior individuals may reasonably expect to be old and senior in the future. If lobbying by senior members (along the lines suggested by Sala-i-Martin and Mulligan, 1999) within unions takes place, this provides then an additional channel along which union’s positions will be in biased in favor of wages and occupational pensions at the expense of junior workers employment levels.

Free rider issues and exclusive services

As any institution providing a public good (here bargaining on wages and labour conditions which will be applied to individuals who are not necessarily union members), trade unions face the usual problem of free riding with respect to membership and active unionism. A straightforward way, for the union to mitigate this problem is to provide additional exclusive services or goods to their members. In this respect, it may be of special importance to union to be closely involved into the management of pensions, unemployment insurance and disability funds. First, because such activities give to the union privileged access to information on procedures, legal aspects and conditions related to the allocation of benefits and pensions. At the worker level, the union can then provide this information and some associated small services (like helping and filling forms), on a discriminatory basis, to individuals who are entitled to these benefits in exchange for union membership and participation.

Also, playing a role in such funds generates top job positions to the union leadership which can be part of an incentive mechanism for promotion and rewards of "good" behavior inside the union.

Finally, participation in the management of benefits or pensions funds gives to the union some leverage in public policy making. In particular, it allows the union to present itself as a defender and manager of workers' rights in general, and to control partly the ideological agenda in society. Doing so may stimulate solidarity towards workers outside the union and to change perceptions on the union's role in society. This may in turn contribute to solve the free rider issue in term of membership and to allow the union to maintain or increase its popular support among workers.

This aspect of participation in benefits funds' management as a device to solve unions' free rider problems may generate a preference for the status quo situation for reform on non wage policies. Unions which, under the *status quo*, are already involved in the management of benefits' funds, will be very opposed to any reform which will reduce their role in this respect. Conversely, unions which are not yet active in such activities may find here a beneficial dimension for which they are ready to make concessions on some other front. But there could be a force in the other direction: a move toward a stronger private second tier pension programme may actually call for more involvement and direct responsibility from trade unions, making them aware of the burden of financing old age protection and of the benefits to union members.

As a conclusion, political economy considerations within unions open up a number of possibilities with respect to the basic set up:

- *The existence of employment protection devices and soft landing plans discriminating (in favor of the insiders, but particularly in favor of the old workers) may produce economic equilibria characterized by high current wage and occupational benefits and high youth-unemployment*

- *In an endogenous-membership setting one can have multiple equilibria, one of this equilibria would be characterized by aging unions, high insider power, high wages and pensions and high youth unemployment*

- The concern for membership may lead the union to provide exclusive services to its members, emanated on a discretionary basis, to be particularly concerned with the governance of pension funds and – most of all – to make a point of preserving the status quo when it comes to pension policies.

2.2.4 Centralized versus decentralized unions' structures

There are a number of political economy issues relevant at the macroeconomic level which should be added to the basic set up. In particular we should take into account general equilibrium effects and the integration of the budget constraint of the government in providing public pensions or publicly funded unemployment benefits.

Once one takes a macroeconomic perspective, obviously an important feature is the budget constraint of the government. ***As we argued, a trade union has an incentive to promote generous public pension systems. First, because it increases directly the welfare of its members. Second, because it improves its outside options and its bargaining power with respect to employers***. Increased public transfers have however to be financed by higher taxes, public borrowing or monetization. In the present European context, monetization is not possible and the public borrowing alternative is quite limited. Remains therefore taxes. How far trade unions will be supportive of generous public benefits depends then on how far they internalize the budget constraint of the government.

In a system of decentralized union bargaining at the sectorial level, sector specific unions will hardly internalize the fact that higher public benefits will induce higher payroll taxes at the level of the economy with negative consequences on employment and income levels. As a matter of fact, much of the taxation burden of these transfers will be passed to other segments of the economy while the gains will be directly felt by unions' members. Each sector specific union will therefore impose a negative externality on the other sectors of the economy (Alesina and Perrotti (1998)). On the other hand, in a more centralized bargaining setting, unions will be more concerned about the welfare of the average worker of the economy. They will be more induced to take into account the basic tradeoff, at the macroeconomic level, between higher public benefits and higher taxes.

Hence one should observe more generous public benefits systems in countries with more decentralized union structures. These same countries should have higher total compensation and higher unemployment. The optimal sharing between current wages and deferred occupational benefits will be biased towards current wages for such economies as public long term transfers partially crowd out occupational benefits. On the contrary, countries characterized by centralized and encompassing unions, will have, everything else being equal, lower unit costs of labour, lower unemployment, and a mix between current wages and occupational benefits more in favor of occupational benefits.

2.3 Unions and Pensions: Empirical Evidence

In this we look more closely at the empirical evidence and on unions' involvement in the welfare state. While there exists a well established literature on the effects of unions on wage growth, wage inequality and employment, very little empirical economic research has been carried out on the action of unions in a broader bargaining framework. A notable exception is the work pioneered by Freeman (1981). First, we briefly review the literature based on research carried out at a micro level, (i.e. making use of data available at individual level for workers and on individual firms), we then provide some fresh evidence of the interaction of unions and welfare by presenting some correlations between aggregate economic variables at a macro level.

2.3.1 Empirical evidence on Occupational pensions and membership

There is a body of empirical evidence that documents how the presence of unions greatly affects occupational pensions provision, both in terms of coverage of workers and in terms of level of old age benefits. In the literature two potential effects have been identified which we discuss at length in the theory : the effect of unions on pension spending corresponding to the union monopoly power raising the total cost of labour (total compensation); the effect of unions on the composition, for a given total compensation, between occupational pensions and current wage. Freeman (1985) and Gustman Steinmeier (1986) show that the presence of unions increases pension coverage. This is due to the fact that unions give more weight to their representative worker whose demand for pensions is higher. In fact, the representative worker is older and more attached to firm and he exhibits higher preference for pensions. It might be hard to distinguish in the data this explanation from an alternative explanation, according to which, unionism increases the probability of attachment to the firm and it increases tenure within the firm, hence making it more likely for a worker to be covered by an OP. Furthermore, unions can monitor the actions of firms in terms of pension policies more than individual workers can do, and it is therefore more likely that unionized plants have OP in place.

In terms of benefit level and scheme arrangements (whether defined benefit-DB or defined contribution-DC) it is hard to draw a definite conclusion on the preferences of unions. We have argued that the total compensation package to employees may be generous if employment protection and soft landing plans are in place. However, because of endogenous membership considerations we could observe equilibria where the concern for employment prevails and total compensation is low (including low OP). Traditional human capital models (Lazear 1979,1983) suggest that there exist a union wage-premium which makes it unlikely for unionized firms to offer DB plans, as there is already an incentive for workers not to shirk. On the other hand union members are usually more protected from firing and therefore this argument could be weak against the long-term perspective of rewarding seniority and offering DB plans[9].

The evidence on OP-coverage for Europe is scanty, but it points to the same conclusions as for the USA literature. Disney and Cameron (1990) make use of cross al data from the Family Expenditure Survey-1984 and find that in the UK union status raises the probability of occupational pension coverage between 8 and 35 percentage points, the strongest effect being among manual worker. Recent calculations carried out on the British Household Panel Survey (BHPS) Wave 7 (1997) relate the presence of unions in a firm to the existence of a pension plan in that firm (the firm to which the employee is attached) and it then relates union membership and OP coverage for that employee. Firm which offer OP are most likely firms where unions are present, and amongst union members there is a high percentage of covered workers.

[9] See Andrietti (2000) for a discussion on this point.

Table 2.1: Occupational Pensions and Union Membership in the UK

	UNION FIRM	NON UNION FIRM	TOTAL
FIRM WITH OP	2139 (88.9%)	1311 (41.25%)	3450 (61.78%)
FIRM WITHOUT OP	267 (11.10%)	1867 (58.75%)	2134 (38.22%)
TOTAL	2406 (100%)	3178 (100%)	5584 (100%)

	UNION WORKER	NON UNION WORKER	TOTAL
OP WORKER	1290 (78.75%)	1296 (32.84%)	2586
NON OP WORKER	348 (21.25%)	2650 (67.16%)	2998
TOTAL	1638 (100%)	3946 (100%)	5584 (100%)

Source: calculations carried out at the Institute for Fiscal Studies (London) on the BHPS, 1997. *Note*: Union membership may be a noisy measure as the question includes staff associations as well as trade unions proper.

We cannot draw any definite conclusion from this simple inspection of the data, partly because we are not controlling for missing variables, (e.g. the size of the plant may be related to both membership and OP provision[10]), partly because of heterogeneity of workers and firms. However, this preliminary evidence is suggestive of the importance that unions attach to OP provisions for their members in those European countries where OP are sizeable. More simply, this is *prima facie* evidence of the involvement of unions in the establishment of pension funds.

2.3.2 Macroeconomic Evidence

There are a number of political economy issues relevant at the macroeconomic level which should be added to the basic set up. In particular we should take into account general equilibrium effects and the integration of the budget constraint of the government in providing public pensions.

Our theoretical model suggests that, in a general equilibrium setting, not only the bargaining framework and the existence employment protection rules may be relevant, but also the internal structure of union members matters. One important dimension of heterogeneity in membership is age (seniority). In particular older unions will tend to favour

[10] Both in the US and in Europe (Andrietti, 2000) there is evidence that larger plants are more likely to offer OPs and they are probably more unionized plants.

the status quo and one would expect that countries with stronger unions and older unions have more generous public pension systems. This is due to both a direct positive effect of pensions on the welfare of union members and to the gains for unions in the existence of an “outside option” that increases the bargaining power of union against the firm.

In the introduction we gave a first account of the variety of old age spending patterns across countries. Figure 1.1 contrasted density and passive membership (percentage of passive members within unions) for a number of countries. While we cannot draw clear conclusions on these patterns, it is interesting to note how, for some countries, density declines while passive membership increases documenting a change in the age composition within unions

Figure 2.1. Old age spending (as percentage of GDP in logs) and passive membership (each variable is related to its 1980 value)

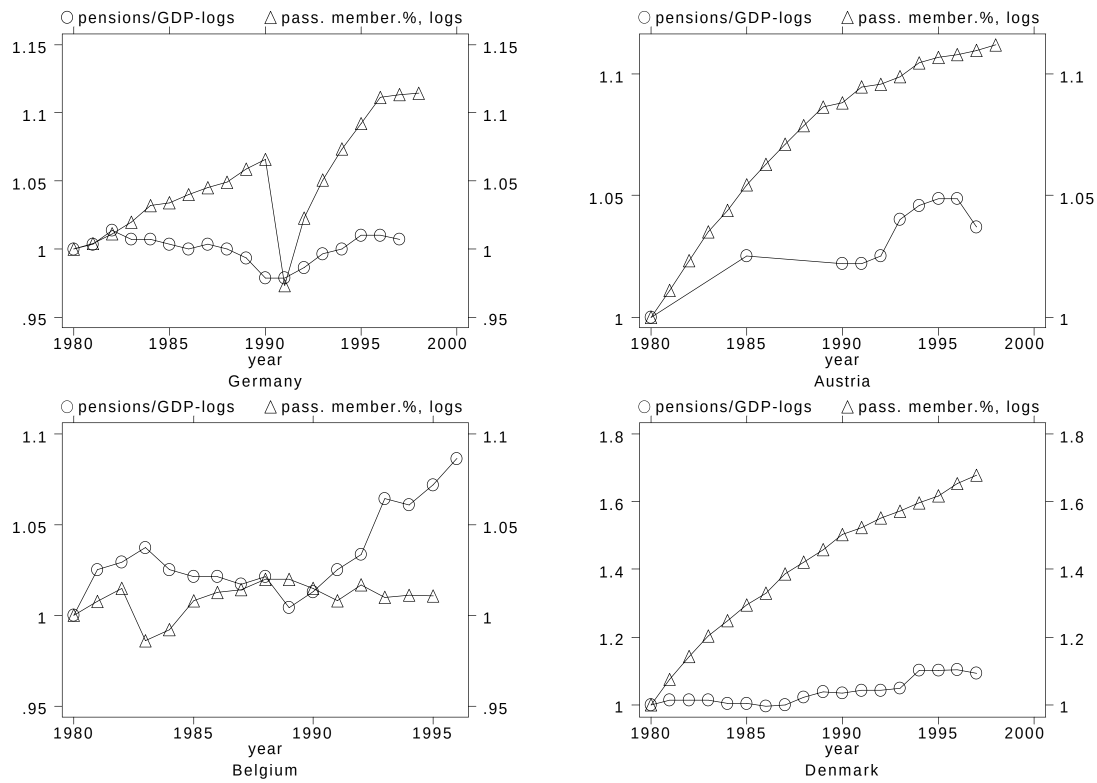
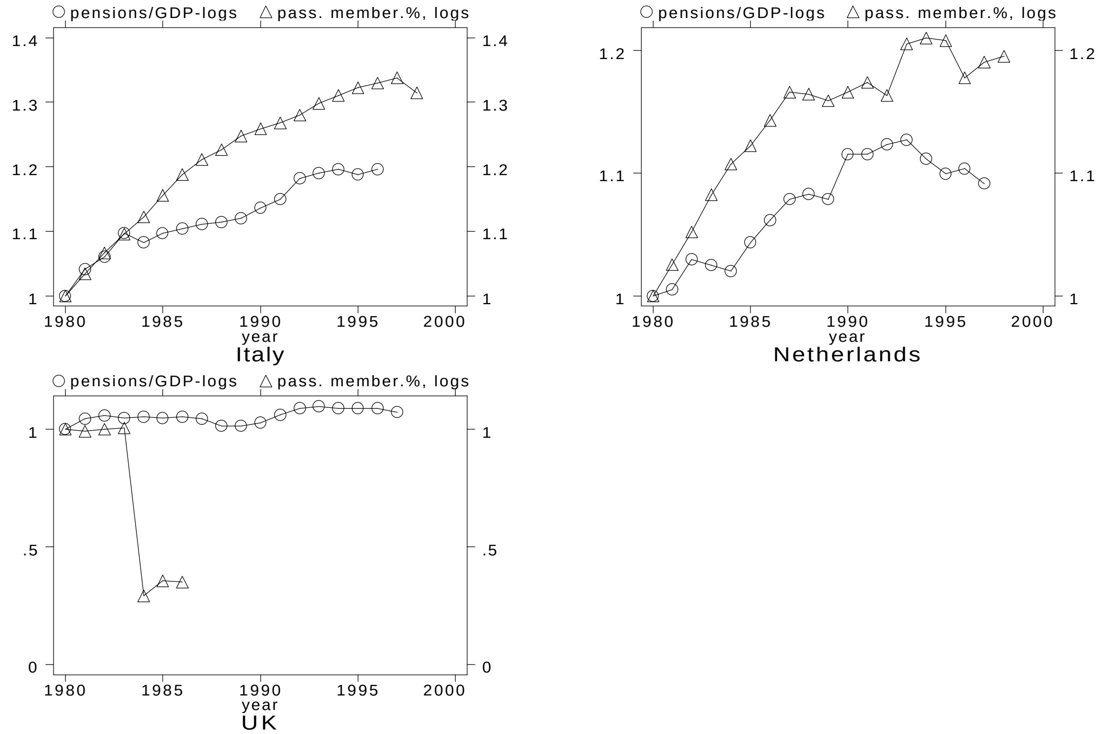


Figure 2.1(continued)



The positive relationship between trends in membership and old age spending clearly emerges when looking at passive membership: not only there exists an underlying common movements in the two series but in some cases we can even strongly relate the cyclical behaviour of the two series (see the Netherlands). However, this might be a partial view of the interaction between the internal age- structure of unions and old age spending. The underlying institutional set up may be a much more robust indicator of the cross-countries variation than looking at changes in policies over time, and we will take up this issue later.

2.3.3 Unions, macroeconomics and soft landing plans.

We argued that employment protection and soft landing plans are relevant in the within-union political economic framework. The existence of employment protection devices and soft landing plans may produce economic equilibria characterized by high current wage and occupational benefits at the expenses of high youth-unemployment. The action of unions, along with government's political decisions, may actually magnify these negative impact on the macroeconomic performance of a country when the full general equilibrium effects are taken into account.

In several countries, governments, facing politically sensitive unemployment problems in declining sectors, have implemented and subsidized various soft landing plans (early retirement, disability, long term unemployment benefits) in order to reduce labour supply. In particular these are restricted to a number of industries, or even firms within an industry, and are typically related to restructuring within the industry. In these cases the eligibility requirements for retirement are less stringent than the general rules. Under these circumstances a worker becomes eligible even if he is younger than the normal retirement age and has a lower number of payroll tax payments (in years) than normally required. Workers have a strong incentive to accept the deal, as this is usually quite generous. We call this situation a ***"pre-retirement option".***

In some respects pre-retirement is fairly similar to collective redundancies, as opposed to individual dismissal. Both are observed at the onset of an adverse shock for the industry (hence the connection to displaced workers) and both affect a number of workers at the same time. The main difference is that pre-retirement offers a soft landing to workers at the expenses of the active population and, ultimately, of tax payers. It is also less unpopular than group firing. Bridging pensions, paid at rates equivalent to the standard retirement pension, with no penalty, have been used extensively non only in Italy but also in Austria, Finland, Sweden, West Germany and the Netherlands (see OECD (1992)). They have often been accompanied by disability pensions. Both schemes have been accepted by unions. Both firms and unions find them appealing because part of the cost falls on the taxpayer.

Generous incentives to early retirement are usually part of public subsidies to private industry. According to Leonard and van Auderdale (1993), government subsidies to declining industries and government paid early retirement schemes are much larger in Europe than in the US. Total government aid to declining industries as a percentage of GNP cost 2.2% of GDP in the European Communities during the late 1980s, with Belgium, Italy and Greece spending substantially over the average.

While displaced workers benefit from the generous treatment provided by bridging pensions, remaining employees and their unions bear little or no cost of the policy. In principle, there is a cost associated to the higher income and payroll taxes required to finance bridging pensions. In practice, these costs are spread over the entire working population and affect marginally the employees of declining firms. Ebbinghaus (2000) documents the potential collusive behaviour between employers and unions existing in this case. Remaining employees and their unions could even benefit from the policy because wage pressure increases. The bargained wage depends not only on bargaining strength but also on the alternative options available to the parties when the settlement is not reached. The availability of generous bridging pensions clearly strengthens the bargaining position of employed insiders.

The Italian experience

In Italy collective dismissals have been regulated since 1991 by Law 223, that was introduced to meet European guidelines. The Law also regulates early retirement due to displacement, that was used intensively during the 1980s by large restructuring firms, with union support (see Barca and Magnani (1989)). Dismissed workers with at least 30 years of contributions have access to seniority pensions (that usually require 35 years of contribution). Initially there was no cost for firms in implementing this policy, and both the anticipated pensions and the missing social security contributions were borne by the taxpayer. It is only since 1992 that firms bear 50 percent of these additional costs. Workers aged between 50 and 59 who have less than 30 years of contributions can still enroll in special mobility lists where they can draw substantial benefits (up to 80 percent of previous pay) for as long as 4 years (in the South of Italy). Their social security contributions are borne by the taxpayer and are measured not as a proportion of unemployment benefits but as a proportion of pay before dismissal. In practice, the large majority of these workers can stay in the list up to retirement. The procedure for access to these lists is bargained with the unions. Union approval is important because applying firms can obtain a rebate on the fixed contribution they have to pay.

Furthermore, unions often favored the “***early retirement option***”. This is embedded in many Social Security Systems (Italy and Spain) as well as Private Pension Plans (e.g. The Netherlands, Sweden, UK). This is a different path for workers to exit the labour market into retirement, though it is not restricted to particular industries or firms and it is completely voluntary. Gruber and Wise (1999) clearly document how the incentives existing within Pension Programmes for early retirement are very strong regardless of the financing-design of the programme itself (i.e. regardless of whether this is of a PAYG financing method or funded – however salary related schemes typically provide stronger incentives).

Precise measures of early retirement are hard to come by. These strongly depend on the institutional setting and on the number of provisions available to workers in old age. E.g., in Italy we observe both pre-pensions granted to older workers in some declining industries in a given time span, and also a very generous early retirement option (which could be claimed at different ages according to gender and to sector of employment). In the Netherlands DI benefits are in practice early retirement provisions (i.e. they are absorbing states). In this sense a more reliable measure of the importance of early retirement is "unused labour capacity" at a given age (see Gruber and Wise,1999 and OECD, 1998). This is simply the fraction of individuals who are not labour force participants at that age. While it properly counts beneficiaries of disability benefits as retirees, it does not account for the unemployed and those in part time work, hence it underestimates the extent of early exits from the labour market in some countries. The available data on unused labour capacity drawn at a micro level (Gruber and Wise, 1999) suggests that a number of countries (notably Italy , The Netherlands and Belgium) have high unused capacity. These countries we also regard as relatively high in union strength.

In general, it is clear that bridging pensions are attractive to dismissed employees and their unions only if pension treatments are generous, at least compared with unemployment benefits. Recall that unemployment benefits are usually phased out after a period of time and often require as a condition active labour market search. They often carry a social stigma that is not associated to retirement.

Beside supporting displaced workers on a discriminatory basis, generous early retirement provisions are a negative externality. They have adverse effects on wage formation and on employment growth. The reason is that, once the government is willing to insure firms against the consequences of business failure, the incentive that unions have to moderate wage demands is reduced by the availability of soft landings (see Calmfors and Horn (1995) for a more general argument). It is standard in the economic analysis of trade union behavior to argue that senior employees, as insiders, have more influence on union decisions than young union members (See Lindbeck and Snower (1988)). A typical outcome of the higher influence of seniors is the presence of LIFO (last in first out) in layoffs (see Freeman and Medoff (1984)). Reverse order of seniority in the selection of dismissed employees shelter insiders from temporary and relatively mild negative shocks. Harsher shocks, however, affects job security of insiders as well, and unions can be pushed to select adjustment measures that insure senior employees against hard landings. These programs have also been supported by employers who find there an easy way to restructure and scale back labour force. Even more, failures to make employers and unions to internalize the true social costs of these programs, may imply significant distortions in terms of allocation of resources and negative growth effects on the economy.

Also, as noticed by Saint Paul (1995), such programs create strategic complementarities between economic allocations and political processes, providing room for the existence of multiple equilibria. Indeed, the overuse of such programs to smooth out the transition of declining sectors, may actually promote the emergence of even more declining sectors, due to the macroeconomic distortions they generate. This in turn will enhance the political demand for such plans. One may end up with two types of equilibria. A ***"high"*** equilibrium with a small number of declining sectors, a moderate political demand for soft landing plans, a moderate implementation of such plans and a high macroeconomic growth rate. But, for very same structural economic characteristics, one may also have a ***"low"*** equilibrium with a large number of declining sectors, high political demand for soft landing plans, overuse of those plans and stagnant growth. Clearly, the possibility of multiple equilibria of this sort is all more likely that unions have relatively decentralized bargaining structures. This kind of explanation may help to explain then the variety of experiences observed by western welfare states on these issues.

Our theoretical model stressed the following points. The more likely seniority rules, LIFO conventions and "soft landing "plans are implemented in the economy, the more likely aging and shifts in the distribution of characteristics of unions towards senior workers implies higher labour costs, higher unemployment and larger occupational benefits. Clearly, going one step beyond, we might also expect the seniority rules, FILO-conventions and "soft landing "plans to be themselves partly endogenous and influenced by the unions' activities. As these mechanisms are generally protecting the old or attached workers rather than the young workers, one may suspect that the same shift in the distribution towards seniority will make these rules more likely to be implemented, reinforcing therefore the conditions under which one will obtain high labour costs, high unemployment (especially among the young or less attached workers) and larger occupational benefits. It follows quite naturally that senior and retiree union members will be able to expand more political influence inside the union than young and junior workers. In terms of our framework, this will imply a pivotal worker with a higher attachment probability than the actual median of the distribution. ***Also, it implies that regimes and rules which favor senior workers and retirees like seniority, FILO, early retirement packages, are more likely to be supported and implemented by the union, with the associated consequences on wages and employment discussed above.***

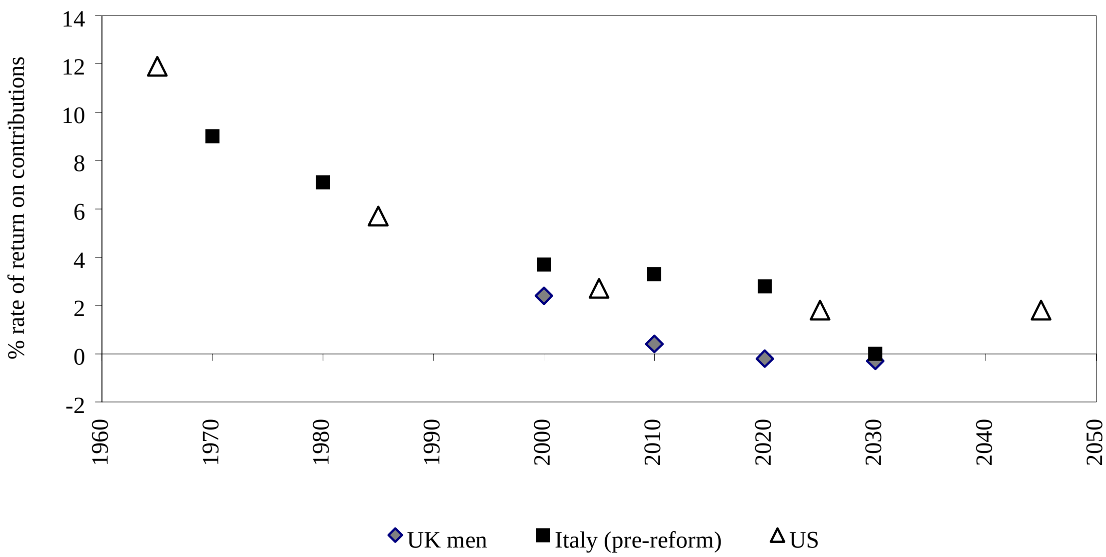
2.3.4 Public pensions, the PAYG Constraint and Intergenerational Effects

If Unions are aware of a PAYG constraint then they know that, whenever the generosity of public pensions – including soft landing plans - increases, this implies higher payroll taxes being levied on workers. The extent to which unions support generous pension plans without suffering negative effects in their membership and without making use of other compensating devices (Bonoli, 1997), depends on how far they can internalize the budget constraint of the government.

Thinking about the Italian example the increased generosity of public pensions happened at a time when gross wages were also growing and hence the budget constraint was not perceived as binding. The conflict emerged during the late 1980's when a quest for pension reforms also developed. The objective is then to avoid loosing younger generations even though they were not the strong group within unions, i.e. membership considerations do emerge. These considerations have to do not only with the financing of generous pension policies via current payroll taxes, but also with the inter-generational redistribution implicit in a PAYG system.

A PAYG funded system implies an explicit redistribution from the young to the retirees. While one tends to impute the intertemporal redistribution to the fact that in a PAYG funding system current pensions are paid by making use of current contributions, this is not the main (or the only) reason for observing this redistribution. If public pensions are actuarially fair and provide the same return as the capital market rate of return, workers will receive in present value terms what they put into the system. However pension systems are actuarially unfair: earlier cohorts of retirees typically obtain a better deal from the system. This is not related to the PAYG nature of the funding system *per se* – it is often due to illdesign and generosity of pension benefits granted to some groups in the population. However, the final effect is that the programme enacts differential treatment for different cohorts participating a PAYG scheme. This fact can be easily documented by looking at the internal rate of return paid by public schemes in selected countries (Figure 2.2.)

Figure 2.3: Real rates of returns to PAYG pension programmes



Source: Castellino (1995) – Miles and Iben (1998).

This redistribution of resources clearly creates tension between generations both at national level and within unions. However, one way out is to guarantee to the young the same conditions as the old in terms of pension benefits. This could work both in society at large and within unions. As long as there is a certain degree of ***inertia or commitment*** on the type of contracts that can be passed between the firm and the union, junior workers will be then less opposed to the preferred wage platform of their senior fellows as they understand that with some probability they might also enjoy part of the wage gains later.

Their incentives to join the union will be accordingly increased. The consequence of this is the fact that, as a political group, the union will have a strong incentive to oppose all type of reform which would break this inertia or commitment device. On the contrary, the union will promote the status quo as this enhances its capacity to bribe young and junior workers to join, without reducing its ability to extract rents through high wages and benefits. One crucial feature is that generosity is to be permanent**.** In Italy this was explicitly made clear during the 1995 major reform of the public pension system, it was named the ***"acquired right principle"***[11].

When it comes to displaced workers, it is easier (and more profitable) for unions to manage a process of exit into retirement while freezing retirement and early retirement rules, rather than an explicit intervention on labour market policies targeted at the young. Hence, once again, a clear tendency to preserve the status quo emerges in early retirement arrangements. We have already noted how internalizing the PAYG budget constraint may not be a problem if a decentralized union bargaining system prevails. In this case the taxation burden is passed on to society at large (i.e. to other sectors) while a quest for old age privileges can be carried out within that sector (Alesina, Perotti, 1998).

But there is an important further observation related to this result. The more centralized is the wage bargain and the more the union can stick to the promise of permanent pension gains, the easier is ***to win young union members to a union policy of generous pension treatments***. Hence, if on the one hand, in a centralized bargaining setting the PAYG constraint should be internalized and the quest for generous pensions reduced, on the other hand, a more compact union can be more credible in its commitment. As observed by Visser (1990), a dominant union has more power and will give more weight to the public good aspect of its objectives, on the other hand – as we argued- an encompassing union is under more strain when trying to externalize the costs of such objectives.

At the same time there could be another process at work, partly mitigating the harshness of the negative effects on younger generations of workers. Again the internal age-structure of unions may mimic the mechanisms operating in society. If seen as a political equilibrium, the support of generous pay-as-you go pension systems require a coalition between the old, who draw benefits but are often a minority, and some other group. According to Tabellini (1992), this coalition involves the old and the poor young (the unemployed). The mechanism works through income re-distribution within households. The poor young pay limited taxes to finance current pensions but obtain income from retired parents, who draw generous benefits. This depends both on the preferences of the old and on the presence of extended families in society. While some young active worker will be lucky enough to benefit, many other will not. Hence it does not always seem appropriate to talk of a

[11] See Section 4 on Unions and Pension Reforms

"workers aristocracy" dominating unions, but rather of some form of solidarity between ***"rich retirees" and "poor non-employed".***

Figure 2.4: Youth-Unemployment and Passive Membership rates

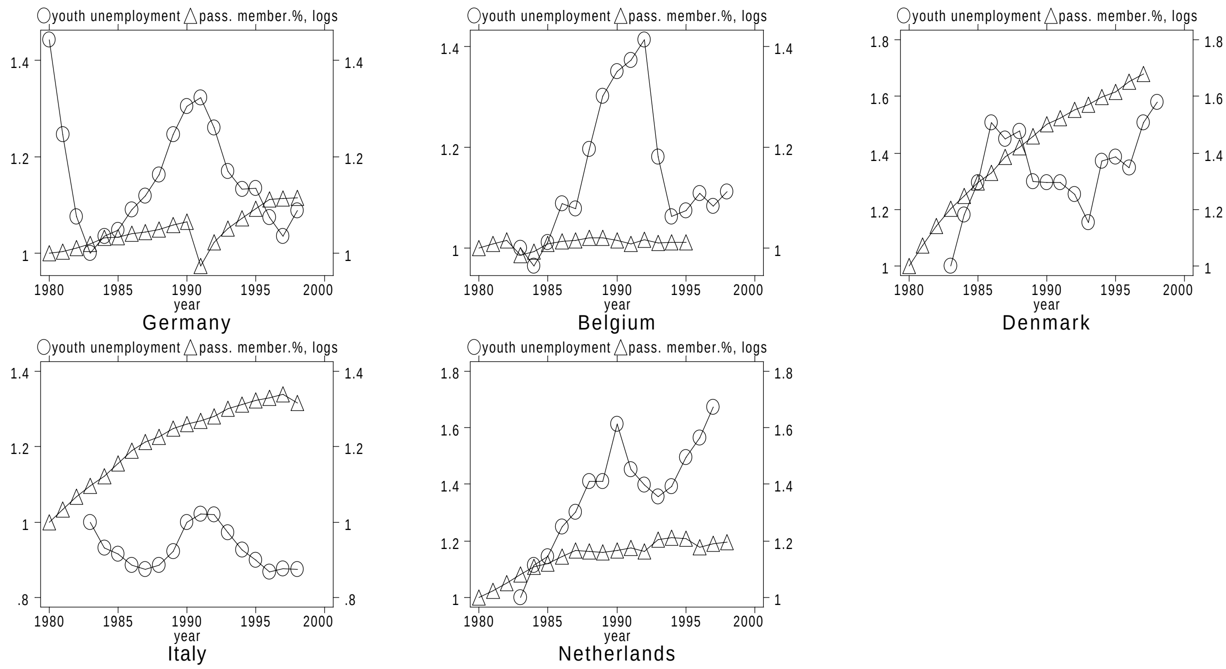
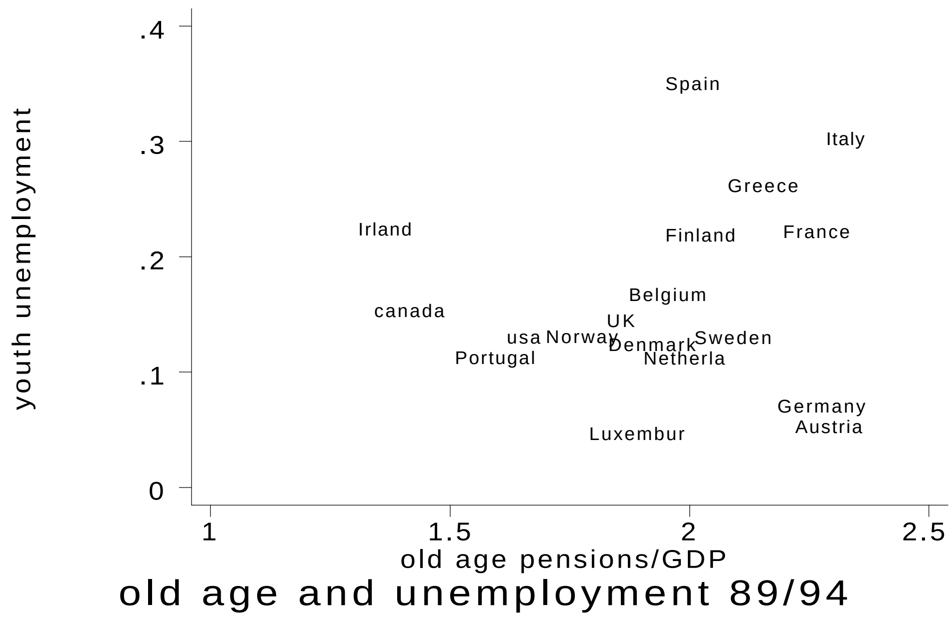
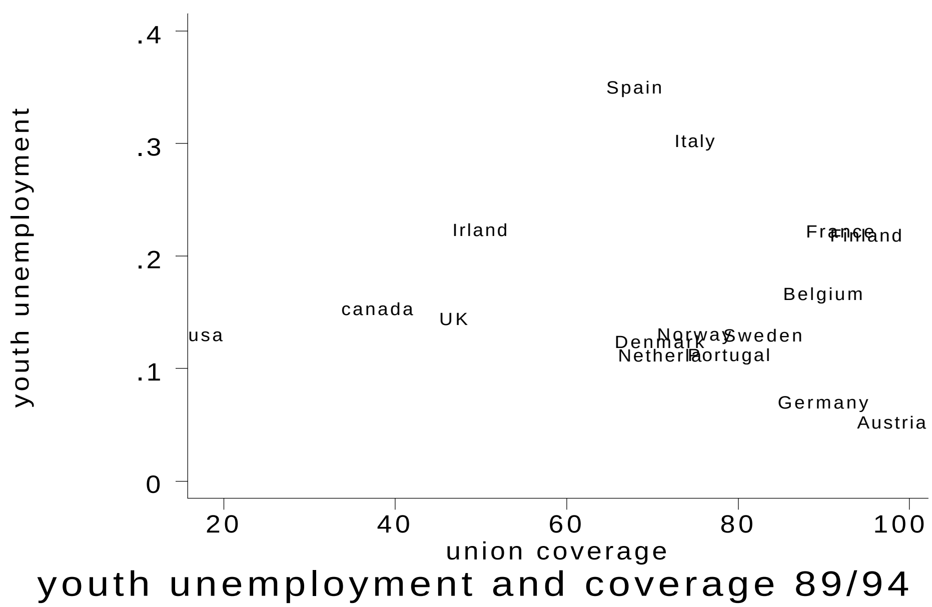


Fig. 2.5: Youth Unemployment and Generosity of Pensions





The interpretation of this set of figures is not simply that the generosity of the pension system "causes" youth unemployment (and this legacy on younger generations would be acceptable because unions are committed to the status quo), but also that part of this generosity is transferred to the "poor young". Hence within family compensation arrangements and labour market institution commitment may help explain why younger generation underwrite an intergenerational contract which is to their disadvantage. Although in the available data we cannot point to a distinct cross countries pattern, we can distinguish some clustering. *Southern countries* like Spain, Greece and Italy at one extreme are characterized by high pension spending, high unemployment and relatively high union coverage, and *Anglo-Saxon countries*, like Ireland, Canada and the USA, at the other extreme, have low pension spending, low youth unemployment and low coverage.

2.3.5 Further empirical evidence.

We have seen a variety of results relating the strength of unions to welfare outcomes. However the theoretical model clearly points to some decision-making by unions as being the result of a full bargaining over wage, employment and occupational pensions (or generosity of public pensions – particularly if public pensions and OP are substitutes). These effects cannot be looked at in isolation. Hence we propose an empirical model which jointly describes old age spending (as a fraction of GDP) and youth unemployment, treating the wage as a joint result of the bargaining process (i.e. as and endogenous variable). This approach builds on Nickell (1997), where the effects of labour market rigidities on unemployment are analyzed. Our main objective is to highlight the role of unions on macroeconomic outcomes going *via* pensions and not to explain unemployment. The latter would require a more complete and richer model of the labour market, which we is not the purpose of the analysis. In this exercise we argue that there is a channel through which the influence of unions operates: unions affect old age protection spending and in turn youth unemployment.

In a first model we want to capture the idea, stated several times in the text, that cross country variation in pension generosity are (1) partly explained by union's strength and (2) that cross country variability in generosity of the pensions system is reflected in higher youth unemployment.

In a second model we relate passive membership, pension generosity and youth unemployment as further evidence that this result has to do also with the internal membership (age) structure of unions. Notice that we include in our econometric specifications the relevant variables pointed out by Peracchi (1999) (demographic structure and labour market conditions) and as emerging from the theory (employment protection rules) as potential candidates for explaining cross-countries variability in old age expenditure. We use two (averaged) time periods and have data for 12 countries. Unions (as measured by union coverage) have a strong positive impact on pension spending, over and above the standard "pension spending" determinants. Union coordination has a marginally significant negative effect. Unfortunately we are not able to provide a satisfactory description of youth unemployment as the positive relationship with pension expenditure (here treated as endogenous variable) described in the simple scatter plots does not emerge as strongly in multiple regression analysis. Hence, while we cannot draw conclusions on the direct and indirect effects that unions have on youth unemployment, as these may be the result of a richer model, our results suggest that strong unions may have an impact on pension expenditure. This is further confirmed when passive membership is used as an explanatory variable.

Table 2.2: Joint determination of Old Age Spending and Youth Unemployment

	Pension-Expenditure /GDP (in logs)	**Youth Unemployment**	**Pension-Expenditure /GDP (in logs)**	**Youth Unemployment**
Log real wage	0.99 (1.75)	-0.17 (0.11)	1.11 (0.71)	-0.092 (0.162)
Dependency Ratio	10.078 (6.057)	-0.601 (0.41)	5.67 (6.45)	0.480 (0.791)
Union Coverage	0.059 (0.016)	-0.0008 (0.001)		
Union coordination	-0.83 (0.52)	-0.03 0.034		
Passive Membership (%)			0.108 (0.024)	0.022 (0.006)
Pension expenditure/GDP		0.023 (0.022)		-0.042 (0.043)
Log GDP		0.004 (0.013)		-0.022 (0.25)
Employment protection		0.007 (0.005)		0.006 (0.009)
Active labour market policies		-0.0008 (0.001)		-0.007 (0.006)
Number of obs	23	23	12	12
R-squared	0.58	0.50	0.75	0.64

Standard Errors in Parentheses.

Source: We integrate the data set used in Nickell (1997) with old age expenditure (OECD) as percentage of GDP (Eurostat-ESPROSS) and data on compensation per employee and youth unemployment (OECD). Dependency ratios are own calculations based on population statistics from Eurostat. Following Nickell (1997), the data referring to unions and labour market structure are based on OECD, (1994a, 1994b and 1995) – and from Ebbinghaus-Visser, (2000). We use union coverage and union coordination, the latter is an index ranging from 1 to 3 and it shows reduced variability for the countries where passive membership is available, hence it was not used in those specifications . GDP is in 1990 Euro and is transformed in logs. Youth unemployment is the unemployment rate for ages below 25. The endogenous variables (real wage and pension spending) have been instrumented by making use of policy variables and demographics. The Sargan test for overidentifying restrictions was satisfactory in the first equation (column 1) but not in the others. Because of a panel element present in the data (2 observations for each country), a GLS procedure would be appropriate. However, because we use instrumental variables, we can only carry out an ex post correction for an AR(1) error component.

3. Learning from welfare reforms: the case of public pensions

The role unions play in influencing welfare policies can be studied in more detail by looking at the current pension reform process across Europe. We have argued so far that unions have tended to defend the status quo of current welfare provisions. As collective organization of their members' interest they are opponents to welfare retrenchment plans which aim at cutting social benefits in order to control social expenditures. Moreover, current pensioners and those that soon expect to become pensioners constitute a sizeable share of the electorate and have higher voter turnout than younger groups: more than one-third of the electorate are in (pre-)retirement age (over 55) in the EU. Given the potential veto points in political decision making and social policy implementation in most European welfare states, as well as the potential threat of massive collective mobilization, unilateral curtailment efforts are thus a risky strategy for governments to choose. Therefore, the potential threat of unrest and strikes could alter a government willingness to negotiate with unions in order to overcome veto points and avoid blame for unilateral retrenchment (Myles and Pierson, forthcoming).

Even where such action would not be likely, governments' reform efforts may be rendered ineffective when the social partners are in charge of self-administration or are running a private collective schemes. In systems were social policy making is shared between the government and social partners, as in France or the Netherlands, tripartite concerted reform efforts are needed in order to guarantee implementation of changes throughout the fragmented and semi-autonomous governance system (Ebbinghaus and Hassel, 2000). In these cases, governments would gain from negotiating welfare restructuration with the social partners and might be willing to engage in political exchange with them. The acquiescence of unions even to painful pension reforms might be possible by offering appropriate side payments in form of concessions in the same or other policy fields. Once the social partners have signed on to reforms, it would be their task to defend the measures vis-à-vis their members, thus the government can avoid or at least share the blame for unpopular measures.

However, why would unions enter negotiations on welfare retrenchment? Indeed, one of the main theme of this report is that unions tend to defend the status quo. Thus, if unions are participating in negotiations over welfare reform, they are first of all interested in defending the acquired social rights of their members and not to sign them off. However, there are cases when union leaders see the need for reform and the long-term positive effects. While cutting the public deficit might be a primary concern of the government, unions may be concerned over the high non-wage labour costs imposed by social contributions which has a negative impact on labour demand. Thus it might well be in the long-term interest of its current and potential future members to sign on to ways of reducing social costs. Thus German unions were in favour of the new Schröder government's effort to cut payroll social contributions by raising green taxes, even if many members might be affected as consumer for higher oil prices.

Moreover, unions may be willing to negotiate retrenchment measures in order to renegotiate the way in which changes occur and prevent more severe unilateral welfare cuts. Thus in the Italian negotiated pension reforms of 1995, the unions were able to bargain longer transition periods for phasing-in benefit cuts and tighten eligibility criteria. They were also able to maintain some seniority rights for older workers and current pensioners, while agreeing to less favourable conditions for younger workers and job-seekers. In such cases, unions may privilege in a political exchange the interest of their core constituency (e.g. senior workers) at the expense of other less represented groups (e.g. younger and unemployed workers). Although the overall outcome of such a reform might still be positive for the public at large, the sharing of reform burden would be place unequally across groups. Finally, concerted welfare reforms often involve larger package deals in which government and employers would receive some concessions by unions in other areas (for instance, wage bargaining) in exchange for maintaining social benefits. Different to the 'old' political exchange of the neo-corporatist income policies of the 1970s, when wage moderation was traded for the extension of social benefits, today's new social pacts involve concessions by the government to 'buffer' welfare cuts (e.g. by largely exempting current pensioners) in return for wage moderation (Hassel and Ebbinghaus, 2000***).***

In this section, we will review some of the main issues and advances in current pension reforms across Europe. A major issue is the reform of the public pension system, given the immediate pressures on labour costs by increased competition and the financial liabilities of the unfavourable long-term demographic development. First, since public pension schemes are by and large pay-as-you-go schemes, a cut in benefits or a rise in social contributions which will upset the solidarity across generations. Unions have to balance the interests of those older members that paid into the scheme in the past and see the current benefits as acquired rights, and those younger and potential future members that will need to pay for the growing number of pensioners and save for their own pensions. Second, a shift from pay-as-you-go to funded systems will create the double-payer problem and thus raise major opposition. Moreover, the current reform plans to expand the second and third tier of pension systems, occupational and private pensions, will pose a difficult choice for unions. Occupational pensions might provide new opportunities to unions to negotiate social benefits that have been previously assumed by state initiative. On the other hand, when unions are weak and cannot negotiate such schemes, a move towards occupational and private pensions would undermine comprehensive coverage, it would also reinforce inequalities already produced by market forces.

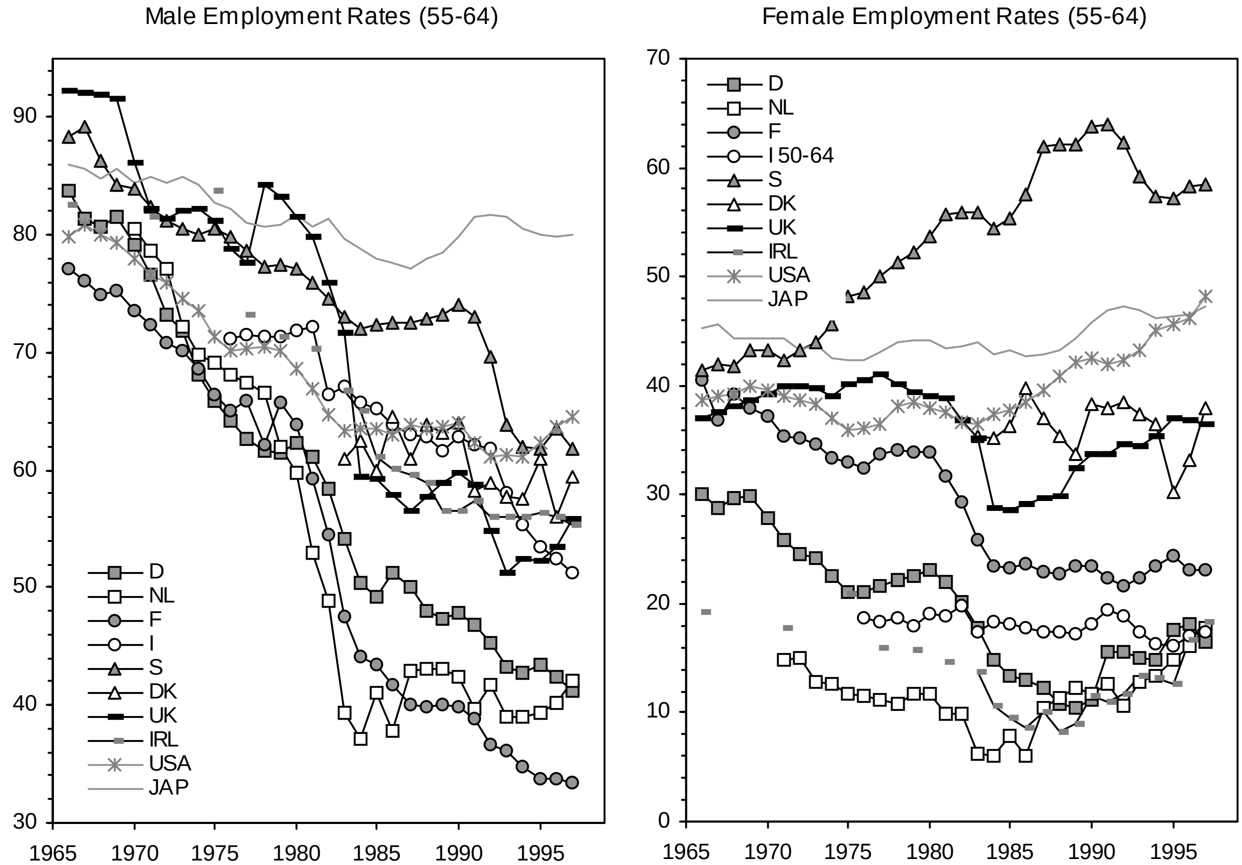
3.1 The long-term and short-term reform pressures

Governments are pressed to undertake unpopular reforms since today's pension systems face major short-term stresses and long-term challenges. The future working population would have to finance via contribution and taxes a higher share of the gross national product for pensions. A shift from PAYGO financing toward funded systems would allow individual private savings, however an unresolved debated is taking place on the advantages and disadvantages of privatization. Many would advocate a mixed systems as the "optimal pension portfolio". Yet a shift from pay-as-you-go to a funded system poses transitional problems: the current active generation would have to pay for the pensions of their parents and grandparents, while at the same time make additional savings for their own retirement. However, some economists (Feldstein, 1998) claim that the double-payer effect for younger cohorts depends on how the new system is phased-in and to what degree the return on capital would outperform economic growth that is crucial under the pay-as-you-go system. In any case, a radical shift from one system to the other does not seem to be viable in any democratic system, however, gradual phasing in of additional supplementary pensions that are fully funded allow a smoother long-term transition. Nevertheless, public pay-as-you-go pension systems remain the main source of old age provision even in countries that have promoted funded pensions.

While the long-term developments of an ageing society may make pension reform timely, yet the time frame of politics is usually much shorter. The odds against major systemic reforms are relative high, and when changes are phased-in to make them less severe, also the benefits will take time to set in. Thus to trigger reform efforts it often needs more pressing, short-term problems such as current deficits of public pension systems that require bailing out by state budget. Such immediate problems constitute a powerful incentive to restore the fiscal soundness of these schemes by a course of fiscal consolidation. Moreover, the pressure for fiscal consolidation was reinforced by the crises of the European Monetary System in 1992 and 1995 as well as by the EMU convergence criteria imposed by the Maastricht Treaty. Since unions also have a long-term interest in the financial soundness of public pension schemes, their resistance towards benefit cuts is likely to be lower if the financial stability of these schemes is threatened. By the same token, unions might acquiesce benefit cuts under conditions of pressing economic crises.

The financing of rising social expenditures is not only a problem for public finances, it has also repercussions on economic competitiveness if payroll and general taxes increase non-wage labour costs or push wages up. Thus unions and employers would have a interest in lowering social contributions, yet they may not be willing to cut benefits from which they profit. In fact, all three major actors, the state, employers and unions, may shift or externalize costs onto the others. Thus in the Germany, past governments have shifted a part of the financial burdens of unification on the social insurance system instead of raising general taxes, while the social partners have used the public programmes to finance early retirement in their own interests, both externalization strategies have pushed non-wage labour costs up (Manow and Seils, 2000). To the degree that early retirement became a pervasive labour shedding strategy in the 1980s and 1990, this passive measure labour market policy, increased the social expenditures even further than demographic pressures alone would have done. Moreover this reinforced the Continental dilemma (Scharpf, 1998): social transfers are paid due to slack in labour demand (unemployment and early retirement), yet the financing via social contribution prices labour even further out of international competition. The renegotiations of financing social security, in particular old age provisions, becomes thus a major issue on the reform agenda, but it is also a relative contentious issue.

Fig. 3.1: Early retirement across OECD countries, 1965-96



3.2 Reversing early retirement

In all OECD countries we find a trend towards early retirement (Ebbinghaus, 2000), but the decline in employment rate among older working people (55-64), especially male workers (see Fig. 4.1) also varies across welfare regimes. It has been least dramatic in Japan and more moderate in the USA, while most continental European welfare states show a dramatic decline, thus the Netherlands, France and Germany (but also Italy) show a significant early exit from work. Today more than every second older men in working age (55-64) has already withdrawn from the labour market. Early retirement in the United Kingdom is less pronounced, partly as consequence of lacking public income schemes. Sweden has had relative high level of employment thanks to partial pension programmes and better integration of older workers in the workforce, though in the 1990s unemployment crisis also Sweden has seen rising old age unemployment. The trends for women are less pronounced, given the traditionally lower employment rate and the increase in participation rates from cohort to cohort.

In nearly all European countries, unions have been lobbying for policies facilitating early exit from work in order to fight old age unemployment due to restructuration and in order to reduce overall labour supply in times of mass unemployment (Ebbinghaus, 2000). Moreover, worker representatives at the workplace supported early retirement policies to accommodate "socially acceptable" restructuration and downsizing, willing to allow a breach of the seniority principle (in collective agreements and employment protection laws). An example is the German and Swedish practices of agreed dismissal of older workers at age 59 or 57, so that they can first obtain long-term unemployment pensions and then disability/preretirement pensions (at 60) and bridge the time till normal retirement age (65). Another examples for collusion by employers and unions are the Dutch collective preretirement insurance (VUT) which were negotiated at industry level by the social partners. Also government policies had facilitated early retirement by special preretirement programmes in the 1980s (Britain and Germany), or by lowering retirement age (as French Socialist government did in 1983).

In light of persistent unemployment and financial constraints, all welfare states sought to reverse past early exit routes over the last two decades. This policy reversal was most pressing in the continental European welfare states, though it was also there that a U-turn proved most difficult in the face of entrenched rights defended by unions, employers' interest in externalising costs, and the possibility of „instrument substitution" presented by multiple alternative pathways (some of which were administered by the social partners at various levels). Indeed, closing down special pre-retirement programs or introducing partial pensions did not bring about much change so long as other, more generous alternatives were available. When governments (often against fierce opposition by unions) succeeded in bringing down replacement rates for public benefits programs, private sector actors like the social partners (or simply employers on their own) frequently filled in the gap between the reduced public benefit and former net wages. Given the veto power of unions, as demonstrated by the French strike wave of 1995, governments sought compromises allowing change to be phased in gradually, since more rapid measures would have adversely affected unemployment.

Higher unemployment and financial constraints also induced the Scandinavian welfare states to put on their emergency brakes. Thus, Sweden departed from its generous disability and gradual retirement programme in 1992, while the Danish government sought to intervene in collectively negotiated pre-retirement schemes in the 1990s. Policy reversal in the liberal-residual welfare states, given the few and limited pathways to early exit, was after closing the special preretirement Job Release Scheme in 1988, largely driven by long-term concerns about demographic trends and their financial implications. Reforms were phased in to restore long-term solvency and remove any incentives to quit work early. Indeed, disability benefits were always limited to cases of total incapacitation and thus would be less a common early exit from work pathway as on the continent.

Hence, while policy makers in all countries (following the policy recommendations of international agencies) seem to be increasingly persuaded of the need to reverse earlier exit policies, they still find it very difficult to change course by implementing „best practices" from abroad. Given the entrenched character of acquired social rights and the continued availability of multiple pathways, social compromises are needed to overcome the social partners' blocking power and insure that some reforms can be implemented, at the very least in that policy space shared by continental Europe and Scandinavia. This will be difficult as long as there exists a social coalition of early exit between firms (which strive for externalising their restructuration costs and circumvent seniority employment protection) and workers interests (which perceive an acquired social right to an early retirement given long worklives, substantial contributions, and lacking jobs). Hence governments will need to bring the social partners into a reform consensus in order to achieve a reversal. This would require the co-operation at several levels (from the national bargaining arena to the workplace) and needs to co-ordinate changes across different public, bipartite and voluntary policies in order to avoid instrument substitution and mere cost shifting from one scheme to another.

3.3 Tax financing or payroll contributions?

Pension systems show considerable variation in financing. Broadly speaking, we can distinguish between tax-financed and contribution-financed schemes, though very often the two are mixed (Hansen, 1999). A truly tax financed basic pension only exited in Denmark until 1994 when an additional employee contribution was introduced. The Dutch general pension, formerly paid by contribution, is since 1990 paid by an ear-marked household income tax which widens the contribution base. Swedish basic pensions are financed by employer contributions and more recently also employee payroll taxes. British basic pensions are financed by employer and employee contributions, though pensions for those without contributions are financed from general taxes. In the other countries, the public pensions are primarily financed out of social contributions, though the state subsidises a considerable share of expenditures, especially solidaristic benefits (e.g. minimum pensions in Austria). In France, in addition to employer and employee contributions, a general income tax has been introduced in the 1990s to finance the 'solidarity' repartition.

Moreover, payroll financed schemes differ in how employers and employee share the costs (see Table 4.1), and there has been major changes over time: in France, Italy and Sweden, the employers have traditionally shouldered the largest share of social contributions. Note that employer contributions while being part of a firm's non-wage labour costs, are not visible to employees in contrast to their own general and payroll taxes. Denmark introduced in 1994 employee contributions in pension insurance, still having very low employer contributions due to the large tax financed share and small earnings related public pension. Sweden increased the employee contributions in the revised public pension scheme by bringing them in line with employer contributions.

While contribution-financed systems give more voice to organized labour and capital and especially benefits paid from payroll employee contributions are perceived as acquired rights, the pressures for reform are also more eminent, given the direct impact of payroll taxes on labour costs. Generally, in contribution-financed systems unions have pressed to cover the financing of non-contributory benefits (such as credits for schooling and child rearing) through higher state subsidies (Myles and Pierson, forthcoming). In contribution-based systems, unions have also a strong interest in stabilising the revenue basis by closing loopholes that allow an opting out of social security coverage. Unions have welcome recent reforms in Austria and Germany to make marginal part-time workers and 'false self-employed' liable to contribution payments.

Table 3.1: Financing of public pension schemes

Country	Method of financing		State	Payroll contribution (% of wages)	
	PAYG	Funding	Subsidy	Employer	Employee
Austria	X		23%	12.55%	10.25%
Denmark	X		100%	—	(since 1994: 8%)
France	X			6.55% of earnings + 7.5% GSG tax	8.2% of earnings + 1.6% of total payroll
Germany	X		27%	9.25%	9.25%
Italy	X		28%	8.9%	24.1%
Netherlands	X				19.3%
Sweden					
- basic pension	X		38%	6.83%	—
- supplementary	X	X	—	6.4%	6.95%
- new system	16%	2.5%*	—	9.25%	9.25%
United Kingdom	X		10-15%	3%-10%°	10%

* of contributions; ° according to earnings level
Source: VDR, 1999; Kalisch and Tetsuya, 1998

In France the creation of a new 'old age solidarity fund' designed to finance non-contributory benefits, was *de facto* a recognition of state's responsibility for non-contributory benefits. This distinction had been a central request of the labour movement in the previous years (Bonoli, forthcoming), while guaranteeing their self-management role in pension insurance schemes. Unions were thus in favour of this reform (despite substantial benefit cuts), since it served their organizational self-interest. By the same token, strategies aimed to cut non-contributory benefits usually meet with lower union resistance than is the case for benefits based on contributions. By contrast, the universal Swedish basic pension, which is not related to individual contribution records, was transformed into a minimum guarantee pension for those that had no or little supplementary (ATP) pension, while the two public schemes became fully integrated in a new pension system that relies now on individualised contributions. The result is a stronger distinction between contribution-related benefits and tax-financed means-tested assistance.

By and large, trade unions have opposed reforms which shift the financing burden from employers to wage earners. This has been a major issue in the recent Swedish pension reform, according to which social contributions should be shared equally between wage earners and employers. As Andersson (1998) points out, this shift was primarily aimed to increase the visibility of pension contributions rather than change the actual amount of contributions paid. Nevertheless, Swedish trade unions feared that not all wage earners might get full compensation through higher gross wages. In order to assure union acquiescence, the minimum earnings ceiling for income taxes was lifted as part of the reform package, relieving low wage workers from the shift in social contributions.

3.4 From pay-as-you-go to more funded systems

As it is shown in Table 3.1, public pension schemes are typically pay-as-you-go. In ageing societies, pay-as-you-go schemes come under pressure to raise contributions to account for increased dependency ratio. An exception is the Swedish ATP supplementary pension which has mixed financing, including publicly controlled reserve funds (largely used for social housing) and the new integrated system which also comprises individual accounts on a funded basis. By contrast, most occupational schemes are funded, the exceptions are the French mandatory supplementary pension, the German public employee scheme, and part of the Swedish collectively negotiated occupational schemes. Some occupational pension funds for instance in Germany, Britain and the Netherlands are defined-benefit schemes, where employers underwrite any deficit that may arise from uncovered benefit claims, hence giving rise to hybrid funding.

The unfavourable demographic development is often assumed to be a comparatively limited problem for funded defined-contribution schemes since these are merely individualised saving schemes, though there might be secondary effects when all baby boomers cash in their stock market gains at the same time in the future. Funded schemes are attractive as they have thus far been able to realise at least until now a higher rate of return than the wage-growth linked or inflation-proof pay-as-you-go systems. But, they clearly entail financial risks. Therefore many unions have voiced criticism about funded schemes, this is, currently so in the French debate on introducing funded schemes. Moreover, unions fear that the growth of pension funds might strengthen the pressure on firms to raise their rate of return at the expense of wage earners, for instance, by further downsizing or by squeezing wages in relation to profits. Unions are therefore often opposed to a shift from a pay-as-you-go /defined benefit to a funded/defined contribution system. When such funds are to be installed, then they prefer to have influence over investment decisions rather than to leave these to employers or trusts. Pension funds could also be selective membership incentive, as it is the case of union pension funds in the USA, though collective bargaining practice in continental Europe would make discrimination between union members and non-union members difficult to uphold.

Experiences in France and Sweden show, how unions' resistance against the establishment of pension funds might be mitigated. In France, the Socialist Jospin government is designing a reorganization of the pension funds that were introduced by its Conservative predecessor and which are so far managed by private companies. The new schemes are supposed to be jointly managed by employers and union organisations. Moreover, to counter fears that the establishment of occupational pension funds would erode the financial basis of the public pay-as-you-go system, contribution to pension funds will not be deductible from contributions to the public scheme (Levy 2000). Most recently, the introduction of individual pension accounts on a funded basis was implemented in the Swedish public pension system (1998 reform, phased in till 2001): the basic and earnings-related pensions will be fully integrated in the new pension scheme, which will be funded jointly by employer and employees (18.5% of wages). As part of the contribution, 2.5% of wages will be paid into personal investment funds. While the unions were basically against the this part of the reform, their acquiescence was assured by the foundation of a state-run pension fund for those unwilling to place their money into a private fund (Nilsson 1998).

3.5 Privatisation by mandated or voluntary occupational pensions?

Of crucial importance for unions is the question whether they can codetermine occupational pensions via collective bargaining or whether these private pensions are voluntary commitments by employers or merely individual private savings plan. Collectively negotiated occupational pensions are now comprehensive in France, but also in most sectors in the Netherlands and Sweden. In Germany, occupational pensions for non-tenured public workers are based on a collective agreement from the late 1960s. Most recently, in Austria and Italy, collective agreements in several sectors established occupational pensions. Voluntary employer plans play a crucial role in the United Kingdom and in the private sector in Germany.

To the extent that public schemes loose the capacity to fully maintain the standard of living during old-age, unions are in favour of compensation trough collectively negotiated occupational pensions. This expands the role of unions in wage bargaining as contributions to these schemes become a part of ‘deferred wages’. Thus Dutch wage bargaining in recent years has entailed wage moderation in return for expansion of occupational benefits. By contrast, voluntary employer plans are part of fringe benefits and are rarely negotiated, giving unions little influence. Instead they have to press for state regulation concerning the vesting and transportability of benefits. Unions also give collectively negotiated schemes preference to voluntary employer plans since the latter typically achieve a much smaller coverage and are often concentrated among white-collar employees in high income brackets. But also the mandatory French occupational system is based on and reinforces the historical division between high replacement schemes for ‘cadres’ (professional and managerial employees) and other lower skilled employees.

In order to overcome the uneven coverage in voluntary systems, unions have been in favour of making occupational pensions compulsory by legislation where they could not achieve the same by collective bargaining. Thus recently, German unions have demanded that if the Schröder government wants to promote funded occupational pensions in addition to the public schemes than they should be made mandatory and financed by employers. In contrast to mandatory old-age provision on a purely individual basis (an option, which is currently under serious discussion in Germany), occupational pensions are typically financed to a large degree by employers. Yet employers insist that occupational pension should remain voluntary fringe benefits.

3.6 Who gets which benefits?

The position of trade unions is also shaped by the degree of occupational fragmentation. The more universal the coverage and the more harmonious the benefits, the more redistribution can be achieved and less discretionary policies can be carried out.. Thus the universal Dutch and the Swedish basic pension leave less space for particularistic interests. By contrast, when public and private systems are fragmented by occupational status lines, there is more potential for rivalry amongst unions. Austria, Germany, France and Italy are cases in point. Certainly, while unions of low income groups might press for a harmonization of benefit levels, other unions are likely to defend the pension privileges of their members. Given the partly diverging interests of unions in a categorically fragmented pension landscape, governments might overcome resistance to pension reform by divide-and-rule strategies, but it may also be difficult to change particularly vested interests.

The fragmented French social security system is case in point. Plans to unify social security failed immediately after the war, the new ‘general regime’ included only private employees (with divisions in supplementary pensions between ‘cadres’ and other employees), while the pre-existing more generous schemes in the public and semi-public sectors remained separate. [12]These different schemes have not only given rise to conflicting interests, they are also amplified by similar organizational splits and aggravated by political rivalry between union movements. Efforts by French governments to harmonize eligibility criteria and benefits as well as to enforce ‘solidarity’ across occupations, that is, financial redistribution among the schemes has met with fierce resistance by vested interests. The reform by the Conservative Balladur government in 1993 circumvented the problem of potential resistance from the powerful public sector unions by confining the welfare cuts to the ‘general regime’ which affects only private employees (Levy, 2000). On the other hand, the following Conservative Juppé government caused major upheavals in the winter of 1995/96 when it announced to introduce similar measures for the special and particular regimes in the public sector: rising contribution period from 37.5 to 40 years (in line with the 1993 private sector reform) and abolishing the early retirement at age 55 under the special regimes. These measures were not implemented, and thus it is now to the new left government under Jospin to establish equality between the two sectors. The recent call by Jospin for negotiations of a ‘pension pact’ that would bring the special regimes in line with the private sector, met the

[12] These over hundred special schemes cover today one fifth of all employees, the large majority of civil servants and utility workers (‘régimes particuliers’) and semi-public sector employees (‘régimes spéciaux’) such as railway employees, miners, and central bank employees (Palier, 1997: 87). Moreover, the ‘cadres’ (managerial and professional staff) in the private sector signed a collective agreement on supplementary pensions in 1947 to maintain similar standards of living after retirement, while lower grade white-collar and blue-collar workers only gradually received negotiated occupational pensions though with more moderate supplementary benefits (on average one third of benefits for cadres) (Reynaud, 1997: 97).

resistance of most public sector unions, claiming that the government should undo the 1993 reform instead of cutting civil servant pensions *(Le Monde* 22/23-3-2000).

Even in universal pension systems without such occupational divisions, governments have been attempting to bring about pension reform by divide-and-rule strategies. They might exploit existing interest cleavages within the trade union camp (for instance, between white-collar and blue-collar workers) that emerge from the differential impact of universal benefit calculation for particular occupational groups. Benefit calculations may differ considerably between various pension schemes, they can be located on a wide spectrum stretching from means-tested / universal flat-rate benefits to purely earnings-related / contribution-defined benefit formulas. The choice of benefit calculation has differential impact on occupational groups: blue-collar workers tend to profit more from flat-rate basic pensions and/or contribution year rules, white-collar employees from earnings-related insurance and/or last salary benefit schemes.

It should not come as a surprise that unions are likely to take different positions concerning the most favourable mix of benefit calculation for their specific rank-and-file. From a ‘fairness’ point of view, one might expect that more encompassing union confederations that represent the general interests of wage earners rather than the particular interests of single industries or occupational groups, should opt for the lifetime principle rather than on the basis of a quite arbitrary number of ‘best years’ or final salary which often results in perverse redistributive effects. In this respect cross-national organizational differences may play out differently: in Nordic countries the peak labour associations are split by collarline differences (blue-collar, white-collar, and academics), in some continental European countries special civil servant federations (Germany, the Netherlands) or autonomous union/strike movements (France, Italy) defend the vested interests of their membership vis-à-vis the more encompassing political union movements. Yet despite the historical institutional and organizational divisions, we do observe a comparatively general convergence towards ‘actuarial fairness’ in the reform of earnings-related pension schemes, all the more since this shift is also likely to strengthen work incentives.

3.7 Unilateral or negotiated reforms?

The British welfare retrenchment is remarkable since it involved unilateral imposition of changes in the pension system . Despite of fierce union resistance, the Thatcher government in 1986 introduced an option to contract out of the public earnings-related pension scheme in favour of private or occupational schemes. Thus, contrary to the experiences in other European countries, the uncompromising style in policy-making pursued by the Thatcher government (in particular vis-à-vis the labour movement) did not result in a failure of the reform, essentially because trade unions were not able to organize support from a large number of current or future benefit recipients against the reform (Bonoli 1999). The unions have also no direct involvement in public pension policy nor in the private and occupational pensions. Thus the government does not need their co-operation for implementation. Most importantly, the political system that provides near unlimited power to the governing majority in parliament allows. Nevertheless, governments have to listen to concerns of the electorate, thus the 1995 pension reform was a reaction to the Maxwell scandals of misuse of occupational pension funds. The new Labour government seems so far not to undo its predecessors' reform, and thus further limits the opportunities for unions to influence the government on welfare policies.

At least outside Britain, the unilateral imposition of pension cuts is likely to trigger substantial opposition from trade unions. Unions have not only more political and economic power in the Nordic and to a lesser degree in continental Europe, they are also considered to be a major proponent and have often an institutionalized role in social insurance systems (see Section 1). This suggests that a policy style characterized by concertation clearly helps to strengthen the prospects for the sustainability of effective reforms. Major pension reform attempts which did not have the acquiescence from the trade unions (Italy 1994, France 1995) failed or were short-lived (Germany 1997) (Ebbinghaus and Hassel, 2000). The social protests in Italy in 1994 and France in 1995 forced the Conservative governments to backtrack in both pension reforms. By contrast, most of the 'successful' pension reforms (Austria 1996 and 1997, France 1993, Germany 1989, Italy 1992/1995/1997, Sweden 1994, 1998, and also Spain 1997 and Finland 1999) were more or less peacefully adopted thanks to interparty consensus and/or consultation of the social partners. These reforms entail various forms of (at least in the long-run) effective expenditure reduction: the link between contributions and benefit was tightened, sharper eligibility rules (especially for early retirement) were introduced, replacement rates were lowered, and the legal retirement age was raised (Baccaro, 2000).

Different to the British unilaterally imposed and partisan reform, systemic reforms without a large societal consensus are not only difficult to achieve in the other European welfare state, they would also not be very viable. Yet not there are different ways in which the reforms of the 1990s have taken into account the different societal interests. In some countries social consensus was achieved primarily through interparty compromise, that is, between governing and opposition parties, though unions could voice their interests within the Left parties and partly the Christian-Democratic parties. For instance, the German 1992 pension reform was based on an interparty consensus between the Christian-Democrats and the Social-Democrats in 1989. After the breakdown of the tripartite Alliance talks in 1995, the 1999 pension reform was largely opposed by the opposition party in 1997 and was later nullified by the change in power to the Left in 1998. In Sweden, after failed efforts of societal committees including the social partners to find a common proposal, the main parties that had supported the initial reform law in 1994 struck a deal in an informal working group without the social partners and was enacted in 1998. Here the parties were the mediators of the conflicting societal interests, and were able to find a common consensus that would be difficult to challenge by either side of the social partners.

The Italian reform process is instructive for the role societal concertation can play were the political system was lacking legitimacy and capability of finding a societal consensus. After failed attempts in the 1980s, the Amato government introduced by decreed in a difficult economic crisis a long-term change in benefit calculations. Only a year later, in midst of the deep crisis of the Italian political system, the technocratic Ciampi government added ad hoc measures that remained small incremental steps, not altering much the ‘acquired rights’, particularly for senior workers. Yet in late 1994 the new Centre-Right government under Berlusconi ‘tried to change unwritten rules of the game that had regulated the Italian social security system’ (Regini and Regalia, 1997: 216), provoking widespread protest by the unions which was able to force the government to backtrack. In May 1995, the new Dini government, supported by the parliamentary Left, was able to strike a deal with the unions (Ferrera 1997: 241). While the law introduced important system changes and stands out to incrementalist policy-making traditions, the ‘key condition for obtaining trade-union consensus was, in fact, retention of the previous pension system as far as more elderly workers were concerned, with the introduction of a new and more rigorous system for workers with lower seniority’ (Regini and Regalia, 1997: 217).

Also the Austrian case is illustrative for the advantages of negotiated reform, it helps not only to circumvent blockage but also blame avoidance. In a remarkable break with the long-term tradition of intense concertation with the social partners, the Austrian government had unilaterally worked out an austerity plan in 1994. This procedure was heavily criticized by the unions. Since the Social Democrats were dependent on support by unionists in parliament, the government was forced to adopt a watered down version of the savings package in 1995. By contrast, the second austerity package adopted in 1996, which was negotiated with the social partners, was far more severe than the first one and covered basically all expenditures of the central state. In the area of pensions, the yearly adjustment of pensions was suspended for one year (two years for civil servants' pensions), eligibility criteria for earlier retirement were tightened and early retirement benefits (also for civil servants' pensions) were lowered. Paradoxically, as Tálos points out, ‘the social partners had gone much further than the government would ever have dared’ (interview cited in Hemerijck/Unger/Visser 2000).

4. Unions and Unemployment Insurance

We have already noticed that the differences in unionization rates across countries seem to have something to do with how unemployment insurance (UI) is organized in different countries. Here we present a more detailed discussion of the interplay between UI and unions. The organization of UI affects workers' propensity to join unions and possibly also wage bargaining and the enforcement of the work test in UI. We also explore how the strength of unions may influence UI polices. Finally, we discuss how UI reforms may be designed so as to encourage wage moderation.

4.1 Unemployment insurance and the demand for union membership

Theoretical issues

How would the organization of UI affect workers' propensity to join unions? It is useful to distinguish between two effects. The first effect works through the demand for union services, taking the (real) wage as given. We refer to this as the effect on membership demand, or simply the membership effect. The second effect might be referred to as the wage effect: the organization of UI may influence real wage outcomes, which in turn my affect workers decisions to join unions.

We outline a simple framework for thinking about membership demand, drawing on Booth and Chatterji (1995) and Holmlund and Lundborg (1999). We think of an economy with industry-wide wage bargaining and open-shop trade unions. Negotiated contracts are extended to all workers in the industry, irrespective of whether they are union members or not. Workers' membership decisions are taken by comparing benefits and costs of joining a union, given knowledge of labour demand and thereby the risk of becoming unemployed. The benefits include union services in general, and possibly UI benefits in case of a Ghent system. The costs include regular membership fees as well as UI premiums if a Ghent system is in place.

Why do some workers join unions and some don't? There are a variety of conceivable sources of worker heterogeneity that may be of importance. Workers may differ with respect to the valuation they place on regular union services, they may differ with respect to access to income sources while unemployed, or they may face different unemployment risks. To simultaneously model all these different forms of heterogeneity is hardly feasible. We focus on the first mentioned type of heterogeneity, i.e., we assume that the valuation of union services vary among the workers. Suppose that the worker compares the expected utility of joining the union with the expected utility of being a non-member. The worker chooses membership as long as the value of membership exceeds the value of being a non-member. Under suitable assumptions, then, there exist a "marginal" worker who is indifferent between the two options. The identity of the marginal worker varies depending on the economic environment, such as the generosity of benefits, the level of UI premiums and the risk of becoming unemployed. The indifference condition for the marginal worker allows us to derive a relationship for membership demand with intuitive properties. We focus on three predictions**.**

(1) First and most obvious: ***the organization of UI matters for membership decisions***. If union membership entails unemployment benefits over and above what is available for non-members, there is an incentive to join a union. If the government in a Ghent country takes a step towards a compulsory system by creating a "basic" unemployment compensation scheme for all unemployed, irrespective of membership status, there will be weaker incentives to join the unions.

In practice, Ghent countries have introduced basic UI schemes in the form of benefits for workers who are not members of the UI funds, but with much lower replacement rates than for those who are members. The extreme form of a basic UI scheme is a system with no benefit differentials between members and non-members (effectively a compulsory system); the incentives to join unions will then of course be even weaker.

(2) The second prediction concerns the effects of changes in the financing of UI. The higher the subsidies to the UI funds are, the lower the UI premiums for the members and the lower the price of joining the funds. Membership would thus rise as a response to more generous subsidies.

(3) The third prediction is that higher unemployment risk raises the demand for membership in a Ghent system. A higher unemployment risk implies a decline in expected utility for both members and non-members, but the decline is smaller for members because of the availability of UI benefits. The attractiveness of membership therefore increases. ***We should therefore expect that union density in a Ghent system rises if labour market conditions worsens, i.e., unemployment rises.*** The direction of the unionization responses to unemployment in compulsory systems is less clear, since there is no obvious reason why higher unemployment risk should change the relative value of membership relative to non-membership in a particular direction.

The fact that workers can, in fact, join the UI fund directly – without joining the union – complicates the analysis by introducing a third option. Direct membership implies absence of costs as well benefits associated with regular union services. The choice between taking the direct versus the union-administered route to the UI fund is presumably affected by the relative costs of the options (the options yield the same insurance benefits). The direct route can be more expensive, as the UI funds (at least in Sweden) tend to charge higher UI premium for workers who have chosen direct membership. This premium differentiation may be the result of higher cost of administration for direct membership, perhaps also a desire to encourage union-mediated membership.

Empirical evidence

There is a large empirical literature on the determinants of union density. The role of the organization of UI has been examined in some of these studies. For example, Rothstein (1990) and Western (1993,1996) use aggregate data for a number of countries and find in their cross-country regressions that union density is substantially higher (13 to 20 percentage points higher) in Ghent countries. Note that the "raw" difference between union density in Sweden and Norway is around 25 percentage points.

It is also interesting to note that the relationship between unemployment and union density appears to depend on the prevailing UI system. Western (1993) uses pooled time series on postwar data and finds that a rise in unemployment induces higher union density in

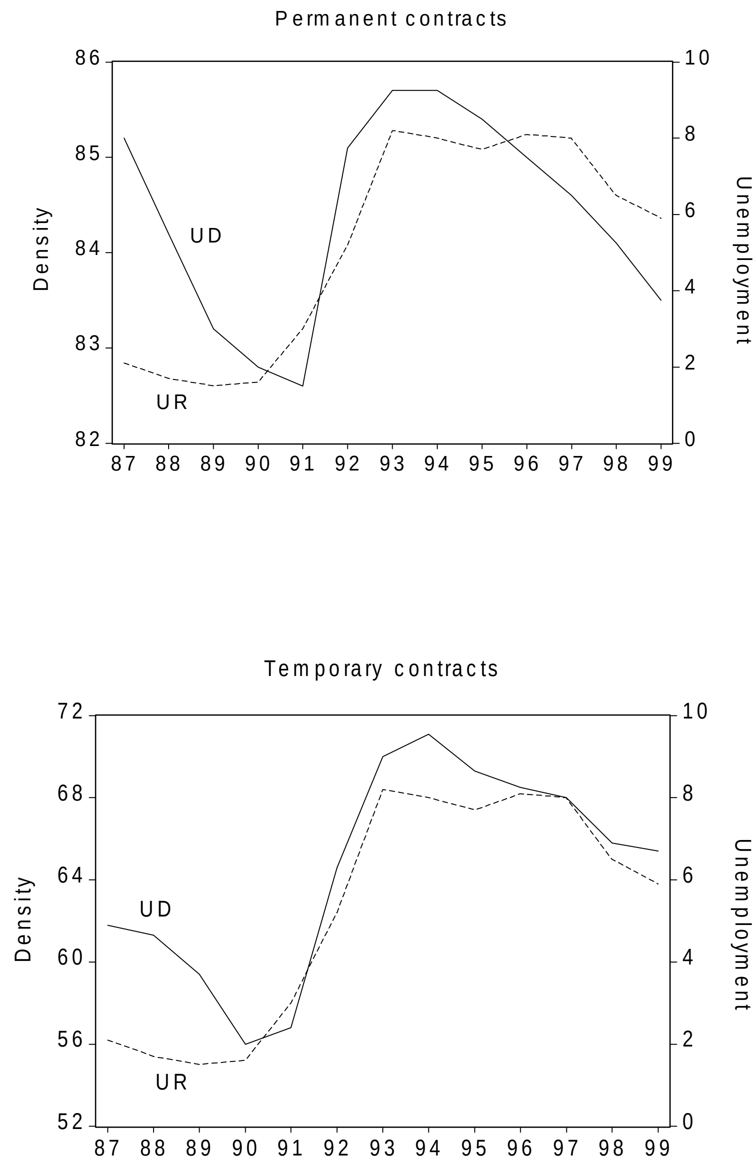
Ghent countries, whereas the effect is negative in other countries.[13] Evidence of positive unemployment effects on union density in Ghent countries are also reported in time series analysis on Finnish data (Pehkonen and Tanninen, 1995) and Danish data (Pedersen, 1982).

Simple "eyeball econometrics" reveal that similar effects are present also in Sweden. Figure 1 plots unionization and aggregate unemployment rates for the period 1987 – 1999. Union density is shown separately for employees on permanent and temporary contracts. The sharp increase in unemployment in the early 1990s is associated with marked increases in unionization rates. These patterns do not seem to be driven by compositional effects, as they survive if we disaggregate by age, gender and sector.

The Finnish experience is fairly similar to the Swedish one. The huge increase in unemployment in the early 1990s – from 3.6 percent in 1990 to almost 18 percent in 1993 – was associated with a substantial increase in union density, which rose from 72 percent in 1990 to 80 percent in 1993. Norway is again an interesting counterfactual. Norway had around 2.5 percent unemployment in the mid-1980s; by 1992 unemployment had reached close to 6 percent. Union density was remarkably stable, however (56 percent in 1985 as well as in 1992).

[13] There is a fairly large empirical literature that exploit time series data in order to uncover the effects on union density of various macroeconomic variables (unemployment, inflation etc). The paper by Ashenfelter and Pencavel (1969) is perhaps the best known early example of this tradition. The microeconomic underpinnings of these empirical models are often weak, however, and the empirical results seem to have been fragile.

Figure 4.1. Union density (UD) and unemployment (UR) in Sweden 1987 – 1999. (Percent of the number of employees (UD) and percent of labour force (UR).)



Sources: Statistics Sweden and Kjellberg (2000).

Changes in the benefit system that affect the relative rewards to union membership in the Ghent system also seem to have effects on unionization rates. The time series analyses by Pehkonen and Tanninen (1995) for Fínland and Pedersen (1992) for Denmark are at least consistent with this claim. A crucial variable in the study by Pehkonen and Tanninen is the relationship between the level of regular benefits (provided by the UI funds run by the unions) and the level of basic unemployment assistance (available for those who are not members of the UI funds). The authors calculate, using their estimated model, that union density would fall by some 10 percentage points if the two unemployment compensation schemes were to be equalized.

The role of UI subsidies for membership demand does not appear to have been subject to econometric analysis. The trend patterns in the data are, however, broadly consistent with the claim that higher subsidies should encourage membership. The difference between unionization rates in Sweden and Norway has increased over time and so has the subsidy rates in the Swedish system.

An implication of a UI system of the Ghent variety is that it encourages union membership also among the *unemployed*, as benefits are disbursed through union-affiliated UI funds. Indeed, the Swedish experience is that unionization rates among unemployed workers who entered unemployment from employment are at roughly the same level as among the employees at work. In 1998, for example, the membership rates were 77 percent for the unemployed and 81 percent for the employed (Kjellberg, 2000). Unionization rates for unemployed new entrants to the labour market are almost certainly lower, however.

4.2 Unemployment insurance, wage bargaining and unemployment

A standard result in most models of union wage bargaining is that higher unemployment compensation raises the negotiated wage. This rise in wage pressure is driven by the fact that higher UI compensation lowers the utility difference between employed and unemployed workers and therefore reduces the cost to the union of wage hikes that reduce employment. The organization of UI, as well as the degree of centralization in wage bargaining, may modify this relationship.

The degree of centralization matters because of the induced tax effect of higher benefits and higher wages. Imagine an encompassing union that experiences a rise in benefits. This union will recognize that the higher expenditure on benefits will require higher taxes. It therefore also recognizes that higher wages will require higher taxes, which will moderate wage demands. ***A similar internalization of the financing of benefits may conceivably take place in a Ghent system to the extent that the union perceives a direct link between the expenditure of the UI fund and the level of the UI premiums paid by the members of the fund. The connection between expenditure and premiums depends on the subsidy system.***

How would more generous subsidies to the UI funds affect wage determination in a Ghent system? There are essentially two effects on incentives in wage setting that loosely may be thought of as an income effect and a substitution effect. The effects are similar to those that appear in response to a change in the tax rate on labour earnings. The income effect is due to the fact that higher subsidies allow lower UI premiums and thereby higher disposable income among employed relative to unemployed workers. This tends to *reduce* wage pressure. The substitution effect arises as higher subsidies reduce the cost to the union of raising the wage, which tends to *increase* wage pressure. The net effect is generally ambiguous, but there is a presumption that the substitution effect dominates so that wage pressure will in fact increase as a response to higher subsidies (Holmlund and Lundborg, 1999).

There is also an additional effect on wage setting that is driven by the induced changes in union membership following higher subsidies. The rise in membership is likely to raise the negotiated wage since a larger membership makes it more difficult for the firms to replace striking workers with non-members, should a conflict occur. This effectively weakens the firm's hand in the bargain, and the negotiated wage increases.

A Ghent system has thus several effects on incentives in wage bargaining. A somewhat simplified characterization is as follows. ***On the one hand, the Ghent system***

encourages union membership and thus strengthens the union's relative bargaining power; wages are thereby increased and employment is reduced. On the other hand, the Ghent system can help to internalize the costs of wage increases and higher benefits. This would tend to encourage wage moderation and increase employment. A crucial prerequisite for the second effect is that the financing system is such that there exists some relationship between higher unemployment in a particular sector and the costs to union members in the form of higher UI premiums. The important element here is the costs of wage increases at the *margin*; a policy that makes the financing scheme such that it increases the marginal costs of wage increases will generally be good for employment. The effect is, in fact, analogous to the effect of higher tax progressivity (cf. Lockwood and Manning, 1993). As is by now well established from a variety of models of non-competitive wage setting, a rise in tax progressivity is conducive to wage moderation.

There are other aspects of the Ghent system that may also contribute to wage moderation. There is a possible "enfranchising effect" arising from the fact that the system encourages union membership among the unemployed. This could potentially increase the influence of the unemployed in wage setting, thus possibly reducing the dominance of employed "insiders". Another possible effect relates to an argument made by Holden and Raum (1991). Their argument is that a large union membership can facilitate coordination in wage bargaining. Since the Ghent system encourages union membership, it may also be conducive to coordinated wage agreements.

There is fairly robust evidence from various cross-country regressions that higher union density (or coverage of collective agreements) is associated with higher unemployment. The most likely explanation for this relationship is the wage pressure effect. To explore whether the association is modified by a Ghent system we have estimated a few equations along the lines of Blanchard and Wolfers (2000). Our baseline model is their first specification where time invariant measures of institutions are interacted with "unobservable shocks", the latter represented by time effects. Our specification is as follows:

$$u_{it} = \alpha_i + \beta_t \left[1 + \sum_j \left(\delta_j + \gamma \cdot G \right) X_{ij} \right] + e_{it}$$

u_{it} is the unemployment rate in country *i* in period *t* (measured as fraction of the labour force). X_{ij} is the value of institution *j* in country *i* (taken as fixed over the included time periods). *G* is a dummy for Ghent countries (Denmark, Finland, Sweden and Belgium, the latter country assigned a value of 0.5 rather than unity). α_i is the country effect for country *i* and β_t is the time effect for period *t*. The effect of a shock at time *t* depends on institutions, and the magnitude of the effect is allowed to vary depending on whether or not the Ghent system is in place. The estimate of γ should be negative if strong unions and generous benefit systems have less adverse effects on employment in Ghent countries.

Table 4.1 displays the results. Note that the variables, following Blanchard and Wolfers (2000), are measured in such a way that the expected signs are positive (except for the Ghent variable). Active labour market policy and coordination are therefore multiplied by minus one. The first column replicates the results of Blanchard and Wolfers and the remaining columns allow for Ghent effects. There is nothing is these results that suggest that the Ghent organization matters for the unemployment outcomes. The estimated Ghent coefficients are far from significant and the signs vary depending on the particular specification. These results are perhaps not surprising considering the very high subsidies of the UI funds in the existing Ghent systems. This means that there is in practice little or no relationship between wage increases in a particular sector and the union members' UI premiums.

Table 4.1. Estimated unemployment equations, fixed institutions. Dependent variable: unemployment as a fraction of the labour force.

	(1)	(2)	(3)
Time effects	.073	.070	.070
Replacement rate	.017 (5.1)	.017 (4.5)	.017 (4.5)
Benefit length	.206 (4.9)	.231 (4.6)	.201 (4.5)
Active labour market policy*(-1)	.017 (3.0)	.024 (1.6)	.016 (1.5)
Employment protection	.045 (3.1)	.057 (3.1)	.045 (2.7)
Tax wedge	.018 (3.2)	.018 (3.0)	.018 (3.0)
Union coverage	0.098 (0.6)	-.017 (0.1)	.107 (0.5)
Union density	.009 (2.1)	.010 (1.7)	.008 (1.5)
Coordination*(-1)	.304 (5.1)	.305 (5.2)	.303 (5.2)
Ghent effect (γ)	--	-.399 (1.0)	.492 (.42)

Notes: The time effects are the estimated time effect for 1995+ minus the estimated time effect for 1960-65. Column (1) replicates the estimates in Blanchard and Wolfers (2000). The other columns include interactions with institutions and a Ghent dummy: column (2) interactions with all institutions and column (3) only with benefit and union variables (replacement rate, benefit length, union coverage and union density). Coordination is measured on a scale from 2 to 6 and is the sum of country rankings of coordination among unions and employers. Coverage is a measure of the coverage of collective agreements (1,2,3). There are 159 observations from 20 OECD countries. Period dummies and country effects are always included. The data are in the form of 5-year averages. Absolute values of *t*-statistics in parentheses.

4.3 How do unions influence UI policies?

How do unions influence policies concerning unemployment insurance? One route works through the administration of UI and the way the work-test is enforced. Another link operates through the political economy of UI: rational citizens voting on UI policies would take prevailing wage setting institutions into account when deciding on their preferred policy. The reason is that these institutions generally affect the employment consequences of a chosen benefit policy.

One can first ask whether there exists an optimal UI policy for a union. Suppose that the benefit level is the only element of the policy and consider a single union in an economy with decentralized wage bargaining. To a first approximation, the union's preferred policy is to set the benefit level as high as possible. The single union has no incentive to consider the tax consequences of its benefit (and wage) choices, since the overall tax burden is the joint outcome of *all* unions' decisions.

Job search considerations can induce the union to prefer a less generous UI policy, at least to the extent that active job search brings some economic return to the members in terms of lower UI premiums as unemployment is reduced. This can conceivably happen in Ghent systems. A similar "benefit moderating" effect can appear if wage bargaining is centralized so that the tax consequences of higher benefits are recognized (analogous to the UI premium effects in Ghent systems).

The administration of UI

If unions are directly involved in the running of the UI systems, they can influence the actual implementation of the UI policies. The Ghent systems are obvious examples. The enforcement of the work test is here in the hands of the labour market offices in cooperation with the union administered UI funds. If a job seeker fails to meet a certain requirement, the labour office should notify the UI fund. It is however the UI fund that takes the final decision on whether a benefit sanction should be imposed (such as a temporary withdrawal of benefits).

A reasonable conjecture is that the strictness of the work test depends on the extent to which prolonged unemployment is financed by the members in the fund or by the taxpayers at large. With current practices, involving very high subsidy rates of the funds (and thus low UI premiums among the members), it is unlikely that the Ghent organization is an instrument that makes the work test more effective than it would otherwise have been. The incentives are weak to encourage search effort by means of benefit sanctions in case workers fail to meet the search requirements. Indeed, the measures of strictness of UI eligibility criteria in different countries, constructed by the Danish Ministry of Finance (1998), do not suggest that strictness differs between Ghent countries and the rest.

Voting over UI

Wage setting institutions may influence UI policies through the effects on voters' behavior. Imagine political decision making in a world with rational voters (and workers) that understand that higher benefits require higher taxes. Voters also understand the moral hazard features of UI: higher benefits will tend to raise unemployment through less intensive search or more aggressive wage demands or both. The more adverse the incentive effects are, the lower the preferred benefits. These adverse incentive effects of UI – the price of UI in addition to the direct tax price – may well depend on the strength and structure of labour market organizations and could therefore affect the choice of UI policies.

The precise relationships between wage setting systems and UI policies are likely to be model specific. It seems reasonable, however, to expect less adverse incentive effects of more generous UI – and therefore higher replacement rates – in economies with coordinated wage bargaining. This should hold because coordination involves internalization of the tax increases needed to finance higher benefits.

A special case with complete centralization of wage setting to an encompassing monopoly union can be invoked to illustrate the point. Ignoring job search, the union's wage choice determines employment. One can then regard the decisive worker as taking two decisions. The wage is set in the labour market and the replacement rate is chosen through the political process. The choice of replacement rate could then be taken without considering the effects on wages and employment (but recognizing the tax consequences). This case would imply close to full insurance, i.e., a replacement rate close to unity.

It is less clear how the choice of UI policies would be affected by the bargaining power of unions in economies with decentralized wage bargaining. Focusing on the adverse incentive effects of higher benefits, the crucial issue is how stronger unions would affect these incentives. In some models, one can find "policy complementarities". For example, the effect on unemployment of a rise in the replacement rate is stronger, the stronger the union's hand in the wage bargain. A popular model, associated with Layard and Nickell and others , can be used to derive an expression for a symmetric-equilibrium unemployment rate of the form:

$$u = \frac{\kappa\sigma}{1-\rho^{\sigma}}$$

κ is a measure of the worker's bargaining power in a broad sense, ρ is the replacement rate and σ, with $\sigma \leq 1$, measures the concavity of the worker's utility function. In this particular example it is clear that a rise in the replacement rate has a bigger effect on the unemployment rate if unions are more powerful ($du/d\rho$ is increasing in the measure of union power).

If such policy complementarities are important, they seem to suggest that the adverse incentive effects of higher benefits should be more severe in economies with strong unions. Rational voters would take these relationships into account in their political behavior, thus opting for less generous benefit systems so as to moderate the adverse incentive effects.

These arguments hinge a number of assumptions that may be violated in reality. It remains to be verified whether one can, even in theory, produce a robust relationship between the preferred UI policy and the bargaining strength of unions. Rather than going into further theoretical speculations we have taken a look at the data. The data are those used by Blanchard and Wolfers (2000). The regressions are based on OECD countries for a maximum of eight five-year periods beginning in 1960. The dependent variables are two measures of replacement rates. The first is the OECD summary measure based on an unweighted mean of 18 different replacement rates for different duration categories and different family situations (see Martin, 1966). The other measure is the replacement rate for the first year of unemployment used by Blanchard and Wolfers (2000).

Table 4.2. Replacement rates and bargaining structure

	OECD summary measure (%)				Replacement rate for the first year (%)			
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Coordination	1.58 (2.20)	.26 (.32)	-.97 (1.05)	-1.43 (1.70)	1.95 (1.93)	1.08 (.93)	-.42 (.32)	-1.03 (.82)
Coverage		6.61 (3.28)	6.61 (3.34)	8.64 (4.68)		4.38 (1.51)	4.37 (1.52)	6.99 (2.55)
Ghent			8.31 (2.63	6.95 (2.40)			10.18 (2.22)	8.42 (1.96)
Dummy For Italy	No	No	No	Yes	No	No	No	Yes
$\overline{R}^2$	.147	.199	.230	.357	.203	.209	.230	.329

Notes: Coordination is measured on a scale from 2 to 6 and is sum of country rankings of coordination among unions and employers. Coverage is a measure of the coverage of collective agreements (1,2,3). Ghent is dummy for the Ghent-countries (Denmark, Finland, Sweden and Belgium, where Belgium is assigned the value of 0.5). There are 160 observations from 20 OECD countries. Period dummies are always included. The data are in the form of 5-year averages.

The results do not support the idea that coordination in wage bargaining is associated with more generous benefits. The coordination-variable is always insignificant once we control for union power by means of an index of the coverage of collective agreements. Union coverage does seem to matter, however; the variable typically enters with significant positive coefficients. The positive signs are at variance with the hypothesis discussed above. The coverage variable varies between 1 and 3, so the estimated coefficients suggest (taken at face values) that up to 25 percentage point differences in replacement rates can be accounted for by differences in coverage. Note also that the Ghent countries have significantly higher replacement rates than the rest.

In conclusion, we have seen that there are some patterns in the data that suggest that the strength of unions may have some impact on the UI policies. Roughly speaking, the data indicate that countries with more powerful unions also tend to have more generous benefit systems.

4.4 UI reforms

The traditional approach to discussions of UI policies emphasizes the tradeoff between insurance and incentives. The insurance motive calls for generous benefits so as to equalize consumption across spells of employment and unemployment. Because of moral hazard, the optimal policy involves less than full coverage of income loss. Moral hazard in the context of UI appears in several guises, the most frequently discussed being the effects on search effort and wage setting. The choice of UI regime may also have important consequences for the degree of unionization.

A UI regime of the Ghent variety can be seen as a device to help unions to overcome the standard free rider problem. The system effectively encourages union membership. The social benefits and costs of (higher) union density depend crucially on the assumptions made concerning the counterfactual, i.e., the nature of the non-unionized labour market. Whereas unions can only make things worse if they enter into perfectly competitive labour market, they can conceivably improve outcomes in a monopsonistic labour market. Standard textbook models of monopsony in "company towns", as well as modern theories of dynamic monopsony, predict that minimum wages over some range can increase employment. A labour legislation that encourages unionism can be regarded as a means to achieve, for example, minimum wages without direct legislation. It is probably not a coincident that there are no legislated minimum wages in Denmark and Sweden, two countries with very high unionization rates.

There is a reasonable case for the view that a Ghent system under certain conditions can be an attractive institutional arrangement. A crucial condition is that the non-unionized labour market is more likely to have monopsonistic rather than perfectly competitive features. A Ghent system, then, can be seen as an institution that delivers (i) UI benefits as well as incentives that in part mitigate the associated moral hazard problems, and (ii) worker bargaining power (and worker "voice" at the workplace) so as to offset monopsonistic exploitation. A condition for mitigation of moral hazard problems is some degree of worker sharing of the costs of UI expenditure, so as to create a direct link between increases in unemployment and the costs to workers in terms of higher UI premiums. Such a link can moderate wage demands by inducing unions to recognize the costs of wage increases.

There is in addition a possible effect working through monitoring of search effort and the enforcement of the work test in UI. The decisions on whether or not to impose a benefit sanction for failure to meet search requirements, for example failure to show up at a scheduled interview with a prospective employer, are taken by the UI funds based on reports from the employment exchange offices. The more costly longer unemployment spells are to employed union members, the stronger the incentives to encourage active search and job acceptances among the unemployed. As we have emphasized, this effect can hardly be of much importance when the UI systems are so heavily subsidized as they are in existing Ghent countries. ***UI reforms in Ghent systems should therefore involve lower subsidies, in particular at the margin, so as to establish a link between UI premiums and unemployment in the sector covered by the collective agreement***.

The role of unions in a compulsory system is less clear. There are in this case no existing institutional framework that can naturally be used to achieve differentiation of UI premiums across workers, thereby influencing incentives in wage setting and search. One might, however, consider US style "experience rating", thereby establishing a connection between a firms' contribution to layoffs and the firm's contributions to the financing of UI. The literature on implicit contracts, pioneered by Feldstein (1976) and others, has explored the role of UI both with respect to the level of benefits and to the financing of benefits. The model features a firm with a pool of 'attached' workers facing uncertain product demand. The firm and its workforce have to agree on a contract that specifies employment, wages and perhaps work hours for every possible realization of demand. The number of laid off workers in each state of demand is given by the difference between the number of attached and employed workers. The model is useful for investigating the role of experience rating in unemployment insurance. In broad conformity with the system practiced in the United States, Feldstein assumed that firms that lay off workers have to finance part of the UI benefits that their workers are eligible to. The model implies that a rise in the UI subsidy - a decline in experience rating - causes a reduction in employment.

The general validity of Feldstein's result has been questioned. For example, Burdett and Wright (1989) have relaxed the assumption of a fixed pool of workers attached to the firm and allowed the firm to choose the number of workers. This modification has important implications. It turns out that higher experience rating does reduce layoff rates but also the number of attached workers. The intuitive explanation is that higher experience rating increases labour costs, which is bound to reduce the number of workers that the firm is willing to hire. The effect on average employment is ambiguous in general, and may plausibly be negative. Finally, it can be noted that simulations undertaken by Mortensen (1994), using the Mortensen and Pissarides (1994) equilibrium model of job creation and destruction, suggest that a fully experienced rated UI tax would increase unemployment, a result driven by the fact that experience rating effectively discourages job creation by making layoffs more costly to firms. The initial claim that experience rating always reduces unemployment has thus not survived later elabourations of the theory.

On the empirical side, Topel (1983) measured the extent of UI subsidization across different states in the United States and found that incomplete experience rating accounted for around 30 percent of all spells of temporary layoff unemployment. Non-subsidized benefits appear to have a negligible impact on layoffs.

There are, of course, good insurance arguments for some cross-industry subsidies in the UI system. An industry-specific shock should not be financed exclusively by workers and employers in the exposed sector. But there are reasonable arguments against current European practices with *no* direct connection between increases in unemployment in a sector and the taxes (or fees) that are used to finance the increase in paid-out benefits. There is a case for increasing wage setters' awareness of the employment-consequences of their decisions. ***Reforms of the financing of UI should attempt to establish a direct connection between the costs of unemployment and the taxes (or social security contributions) that are raised to cover the costs of higher unemployment.***

UI reforms involving some degree of experience rating raises a number of practical issues. Although it is conceptually straightforward to link employee (or employer) contributions to sectoral unemployment, it may be difficult to do so in practice. Bargaining areas typically coincide with industries, but unemployment rates by industry are not well defined concepts (and data are often lacking). The most practical approach is probably to make use of information on benefit receivers and their previous employers, as in the US system of experience rating. The contribution to UI financing – from employers and/or employees – would then be linked to the firm's contribution to UI expenditures. This would clearly increase the cost of job destruction. However, it is important to provide incentives for job creation as well. This can be achieved by making the contributions dependent on the duration of benefit receipt. On the firm side, this imply incentives to rehire unemployed workers. On the union side, this also provide incentives to promote job finding activities among the unemployed, thereby reducing the employees' contributions to unemployment support. UI reforms that involve some experience rating can alert union members and union leaders to the social costs of excessive wage increases and insufficient job search.

4.5 How Would a Ghent System Help Other European Countries?

The analysis of this has shown that a union administered UI scheme is not correlated with higher unemployment (Table 4.1). Further, we have observed that "Ghent countries" tend to be characterized by significantly high replacement rates (Table 4.2), which, in turn , are positively correlated with unemployment (Table 4.1). These findings suggest that if a Ghent country were able to keep its replacement rate under control, the introduction of a Ghent system would not adversely affect the unemployment rate, and the Ghent systems could play other important roles. Such roles refer to the unions' ability to organize workers covered by temporary contracts, and the unions' ability to impose benefit sanctions on unemployed workers that reject job offers. In what follows, we discuss both such roles.

An important effect, linked to the existence of Ghent systems, is the possibility to prevent the emergence of a dual economy, a phenomenon typical of Southern European countries. In France, Spain and Italy, we observe a growing proportion of workers employed in jobs whose contract is regulated by a temporary contracts. Clearly, the interests of this growing fraction of workers are not easily represented by the trade unions, and the conflicting interest between the protected insiders and the unprotected outsiders represents an important challenge for Southern European Unions, whose action appear often in contrasts with the interest of workers employed in the secondary labour market. Further, the workers employed with such temporary contracts tend to be younger workers, further amplifying the intergenerational conflict in the area of welfare reforms. The evidence presented suggests that in Sweden, union membership is high not only among regular workers, but also among workers whose employment contract is temporary in nature (Figure 4.1). Thus, it may well be that a union-administered UI scheme would be a way for establishing an institutional contact between unions and temporary contracts, since the latter workers are the most likely beneficiaries of the UI benefits.

Further, existing evidence presented by the OECD (OECD 2000) suggests that unions led UI may be particularly well suited for imposing benefit sanctions on unemployed workers that refuse to take up a job offer during an unemployment spell. While we can not provide definite evidence on this relationship, it is remarkable to observe that Belgium and Denmark are the only countries that impose a full exclusion from unemployment benefits in the aftermath of two refusals of job offers. In as much as this conjecture will be confirmed by further research, the Ghent system may appear to be a very good way to reduce search disincentive linked to long lasting unemployment benefit.

5. Conclusions: What do Unions Do to the Welfare States?

5.1 Do unions interact with the welfare state? How do they do it?

In this report we observe that there are wide differences in unionization rates and welfare policies among industrialized countries and we document recent trends on both these dimensions.

Variability in the prominence and the activity of unions is obviously explained by the model of organization of labour and the employer-union and government-union relationship existing in each country. However, union density and the composition of union members, particularly composition by age, vary widely across countries also as the result of very distinct trends of the recent past. During the 1980s union density fell sharply in a number of countries, whereas it remained stable or increased in other countries. By 1990 union density had dropped to 15 percent in the United States and to 10 percent in France, while it had increased by 10 to 20 percentage points in all Nordic countries except Norway. On average union density among OECD countries stood at 43 percent in 1970 and had increased to 47 percent in 1980. By 1990 it had fallen back to 41 percent (OECD, 1994).

There also marked cross-countries differences in terms of welfare policy design and social protection spending. Social protection expenditure was high in the early 1990’s in countries like Sweden and Finland (ranging from 39 percentage points of GDP to 29 percent of GDP) while countries like Portugal and Spain spent 16 percent and 22 percent of their GDP. In terms of composition old age benefits are a prominent share of total expenditure in Italy, Austria and Portugal while Nordic Countries spend considerably on labour market policies. This difference in spending patterns cannot be explained solely in terms of population aging, relative welfare positions and labour market shocks characterizing these countries.

We propose a taxonomy which distinguishes four regimes of industrial relations and similarly four welfare regimes, namely *Nordic Countries* (Sweden, Finland and Denmark), *Continental Countries* (Austria, Belgium, France, the Netherlands and Germany), *Anglo Saxon Countries* (UK and Ireland) and *Southern Countries* (Greece, Italy, Portugal and Spain), though some countries are rather hybrid cases (e.g. France and the Netherlands). This allows us to better understand the patterns in union characteristics and welfare spending observed in the data. On a scale which takes account of both generosity and comprehensiveness of social security, most Nordic countries occupy the top position followed by the Christian-Democratic social security states of the Continent (Austria, Belgium and the Netherlands). A third cluster is represented by the rest of the Continental states, while the Anglo Saxon welfare states and the Southern countries are at the bottom of the scale. Also, qualitative and quantitative indicators point to the Scandinavian countries as being characterized by the highest unionization levels and union coverage, while Anglo Saxon countries are at the other extreme. The rest of the states we were able to classify are somewhere in between these two extreme cases and have experienced different cycles in industrial relations dynamics. On the basis of this taxonomy we find, on average, a positive relationship between union movements and the expansion of the welfare states, particularly in the 1980's and early 1990's. Yet the relationship is not always clear, some countries are interesting outliers: they have well developed welfare states and low union density pointing to additional institutional factors affecting this relationship.

One important dimension, which is lacking from the simple correlations described above, is the extent to which trade unions influence welfare outcome and how they exert control over welfare policies. Indeed this seems the key factor to explain many of the stylized facts highlighted above. Trade unions often overlap with political movements and different political legacies may play a direct role in the actions of labour movements hence explaining their concern for welfare policies. Another route of trade union involvement in welfare policies emerges when considering trade unions as self-administration institutions in social policies. While this may not necessarily have an impact on welfare design, as welfare policies and reforms are often set by central governments at national level, trade unions may be effective in counteracting policy changes in their actual implementation, especially when benefits are provided in a fragmented and corporatist fashion. The interaction of institutional settings, industrial relations and welfare outcomes is best seen in the provision of old age insurance. Unions are typically involved in the establishment of occupational pensions through collective agreements. In these cases, and in general when a funded component of pension provision is relevant, there exists a more direct link between contributions and benefits, which implies that unions have less incentives to unload on society at large generous pensions policies. At the same time rent-seeking activities may be more pronounced the more fragmented is the pension programme and the larger the number of public or private funds existing in the economy. Finally trade unions have an institutionalized role in political decision-making: even if the direct impact on actual law-design may be negligible, the position of unions may shape public debate or even provoke collective actions.

5.2 What are the effects of union actions on welfare outcomes?

On the basis of these stylized facts we develop an economic theoretical model shows some novel features of the bargaining process of unions by recognizing the importance of the internal seniority structure of unions and the concern for membership. The economic model assumes that pensions are part of the compensation package and assumes that unions enjoy monopoly power, but looks more specifically at the insurance role of unions in a broad bargaining agenda. This sets the basis to look both at the microeconomic implications and the macroeconomic considerations of the effects of unions on welfare and on labour market outcomes.

We find that unions may mitigate market failure effects on workers due to the existence of imperfect insurance and credit markets. So in this sense, unions may be significantly welfare improving. At the same time however, the political economy of unions suggests that there are strong presumptions that unions will bias reform processes towards the status quo situation. Hence one can observe at the same time a strong seniority bias by trade unions in both preserving the status quo on generous pension arrangements and favouring soft landing plans for older workers – possibly at the expenses of younger generations. This position may entail important dynamic inefficiencies in the sense that changes in economic conditions which necessitate changes in policy regimes may not be accommodated by governments because of lack of support or veto power of unions. Obviously this may more likely occur when unions are less encompassing and less representative of the general working population. Also this is more likely when unions and governments do not face clear commitments on future policy outcomes.

Indeed our empirical evidence points to a positive relationship between union strength and old age spending, after controlling for those variables which typically affect old age benefit provisions in the economy . This result confirms the view that unions tend to support generous old-age protection policies and justifies the finding that they generally oppose retrenchment. This correlation with old age spending is particularly strong when looking at the variation in passive membership, i.e. the percentage of older (even retired) union members. Furthermore, myopic behaviour on the side of unions may have prevailed up to the mid-1990's and may have contributed – via old age spending and spending on "soft landing plans" - to the negative performance of the economy in terms of unemployment in several countries.

5.3 Which model of union better resolves the trade-off between welfare-enhancing activities and rent-seeking activities?

We look at a unique experiment, carried out in several European countries (namely some of the Nordic countries) in the provision of unemployment insurance. This unemployment insurance arrangement is referred to as the "Ghent" regime. It is a union-led provision, which is government subsidized but union administered, and it clearly brings out the direct involvement of unions in the self-management of insurance against labour market risks. While the concern for membership clearly points to a preference of unions for this type of exclusive arrangement, a special feature of the Ghent system is that it may encourage unions to internalize the budget constraint implicit in the financing of unemployment benefits. In fact trade unions are led to perceive the link between the spending on unemployment benefits and their generosity and the funding of these expenditures, depending also on the level of subsidies coming from government financing. This increased responsibility may lead to moderation on wage bargaining and more favourable conditions for labour market outcomes. The additional positive effect may come – at a microeconomic level - from the degree of control that unions may exert on unemployment benefit recipients. Unions may help reducing the typical moral hazard problem affecting these provisions trough monitoring of search efforts. One important conclusion is that these beneficial effects are much less effective the more the system is subsidized from external finances. Reforms aimed at changing the financing of unemployment insurance should attempt to establish a closer connection between the costs of unemployment and the taxes (or social security contributions) that are raised to cover those costs. This would increase the awareness on the side of unions of the employment consequences of their decisions.

Further, our report argues that the existence of Ghent system may counteract the emergence of a dual economy, whereby a growing number of workers employed in temporary contracts become insulated from union influence and from the insurance schemes provided by the welfare states. The evidence presented suggests that in Ghent countries, union membership is high not only among regular workers, but also among workers covered by temporary contracts. Thus, a Ghent system may be way for establishing an institutional contact between unions and temporary workers, since the latter are likely to be very interested in unemployment insurance schemes. This, in turn, would help addressing one of the main challenge faced by unions in Southern Europe.

5.4 Is it possible to win the support of unions in reforming welfare systems?

We ask whether unions will take a true "solidarity" approach in negotiating reforms. Due to necessity of tightening of the public spending budget constraint and to the potentially harmful consequences of financing generous social protection expenditures, unions seem to become increasingly aware of the consequences of opposing welfare cuts.

The interest of unions in welfare reforms, particularly curtailing of old-age spending, is explained in our theoretical model as tendency to preserve the *status quo* and defending acquired social rights due to internal membership concerns. In other words unions exhibit a seniority bias not only in wage setting activities but also in the interaction with welfare policy. When unions are directly involved in negotiating reforms this seems to be the norm. However, government's reform efforts may often be rendered ineffective when unions are in charge of self-administration or when they are directly involved in the management of pension schemes: as we argued above, unions can prevent the implementation of unilaterally decided changes. In these cases governments seem to gain from negotiating reforms involving welfare retrenchment by engaging in political exchange with unions on other policy fields.

However there are examples of the potential advantages of winning the support of unions in the area of pension policies: in some cases unions have adopted a forward-looking behaviour and have recognized the long term benefits to the economy at large of welfare restructuring. For example German unions were in favour of the recent government's efforts to cut payroll social taxes. The recent pension reform in Italy is somewhat controversial. It is a case where the dynamic inefficiency effect of unions still played a key role and yet a major benefit-reducing and expenditure-stabilizing reform was supported by unions, at the onset of European monetary integration. This example contains the main ingredients of our results: the prospects of monetary integration provided credibility to the tightness of the government budget constraint, this helped the unions to generate realistic expectations on the dynamic evolution of the status quo point and induced them not to oppose the reform process. On the other hand, unions were able to bargain to maintain some seniority rights for older workers and retirees at the expenses of less represented groups. One conclusion of this report is that the challenge for unions is to become a progressive force in society and that it is a socially desirable outcome to prevent the decline of unions. Trade unions can achieve this goal by moving from one economic/political equilibrium where their actions are driven by a seniority bias to an equilibrium where they are directly involved in the administration of unemployment insurance and in the growth and management of second-tier occupational pension plans. This role of unions may ultimately win back membership and loyalty of younger workers and may strengthen their long-term credibility.

Table A3: Chronology of Major Old Age and Disability Pension Reforms in the 1990s

Country / Year	Reform	Role and position of unions
Austria		
1996	'Sparpaket' (austerity package: early retirement benefit cuts, benefits frozen)	Grand coalition negotiates with social partners (prior to EMU)
1997	long-term phasing in of cuts in early retirement pensions and harmonization of public sector pension provisions with the less generous pensions schemes in the private sector	grand coalition negotiates 'last minute deal' with social partners
1999/2000	increase of retirement age, cuts in early retirement (not yet enacted)	union oppose (breakdown of grand coalition, similar plans of right government)
Denmark		
1989+	Establishment of collectively negotiated occupational and earnings-related pensions; pension funds are under supervision of bipartite boards	Unions have changed their opinion in favour of a multi-tier pension system
1994	general income tax on pensions in combination with higher gross pensions	
1999	cut in early retirement benefits and normal retirement age lowered from 67 to 65, employee contributions to efterlon scheme	interparty compromise, criticism by general workers union (SiD), demanded legal guarantee of employee rights
France		
1993	Balladur (private sector pension) reform: 40 instead of 37.5 years in contribution; 25 instead of 10 best years	consultation with unions, unions in favour of new state subsidy but most were against cuts
1995	Juppé plan: similar cuts in public sector schemes, ending of favourable early civil service retirement; also budget control by parliament	unions opposed (fear of changes in self-administration), massive strike wave in defense of status quo, government back tracks except for budget control
1997	Robien law: introduction of private pensions (new Jospin government repeals act)	offers in 2000 negotiations on outstanding reforms, most unions are opposed
Germany		
1989	1992 reform (enacted in 1989): shift from gross to net wage indexation, phasing out of early retirement options, increase in retirement age for women (from 60/63 to 65)	interparty consensus after consultation with social partners
1997	1997 reform: faster phasing in of cuts, introduction of a demographic factor in benefit calculation	unions end tripartite talks after centre-liberal coalition announces austerity plan in 1996,
	Raising the financing share of the state	
		limited agreement with opposition
1999	new red-green government annuls demographic factor, but for two years lower pension adjustments, future reform still needed	unions criticise adjustment (though protest is limited) , metal worker union wants wage fund for early retirement at 60 (employers opposed)

Table A3 (continued)

Country / Year	Reform	Role and position of unions
Italy		
1992	Amato reform: phased in increase in retirement age, contribution periods, contribution rates	consultation with unions
1993	Ad hoc measures: freeze of seniority pensions	
1994	Berlusconi plan: faster phasing in, seniority pension freeze, fails with severe cuts	unions mobilize against cuts, Conservative government looses majority
1995	Dini reform: change to actuarial contribution-defined benefits, phased in changes to harmonize rules and tighter eligibility, especially of seniority pensions	agreement with major union movements (confirmed by membership vote but unpopular with workers) , employers criticise concessions to unions
1997	faster phasing in of new benefit formula, seniority pension cuts harmonized (but blue-collar workers are exempted)	negotiations with social partners, Communists MPs oppose seniority pension cuts, get exemption for blue-collar workers
Netherlands		
1991	reform of disability pensions and sick pay system	major demonstration, internal opposition in government parties (grand coalition)
1992	linking of benefits to active/non-active ratio	(unions will have to internalise the negative employment effects of wage increases)
1995-97	early retirement schemes (VUT) become funded, civil servant pension fund privatized, reform of governance system	unions renegotiate VUT agreements to fill in replacement gaps, left-liberal coalition intervenes in governance structure
Sweden		
1991	end of disability pension for older unemployed	
1996		LO-SAF agreement to change blue-collar occupational pension to funded system
1998	new pension system plan: gradual increase in seniority age, minimum age, benefits based on working life earnings, introduction of funded individual accounts	interparty consensus (Conservative government and Social Democratic opposition); principal acquiescence from unions
U. K.		
1988/89	1988: begin of private individual pensions (AVC), diminished benefits of state earnings-related scheme (SERPS); 1989: end of special early retirement scheme	Sharp criticism from unions
1995	Pension Act: minimum solvency standards for private pension funds and compulsory indexation	public pressures after Maxwell bankruptcy affair

Sources: compiles from EIRO, EIRR, MISSOC and various other sources.

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