Pension politics and policy in Denmark and Sweden: Path Dependencies, Policy Style, and Policy Outcome

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Abstract:

The paper compares recent reforms of the Danish and Swedish pension systems which started from a common point of departure but has moved in increasingly different directions during the last decades. Focus is on the mechanisms of path-dependent change behind these reforms which seem to confirm the prediction that flat-rate universalism will eventually produce dualism and new dynamics (but for somewhat different reasons than commonly believed) but also indicates that Swedish universalism was inherently unstable. Next, the paper compares the extremely different decision making processes behind the reforms in these two countries. Finally, it is discussed to which extent the different institutions are nevertheless likely to produce equivalent outcomes in the future.

1. Introduction: From Convergence to Divergence

Although Denmark and Sweden are usually considered members of the same family of welfare states - the universal or Social Democratic welfare regime - their old-age pension systems have moved in highly different directions during the last decades. Both countries started out from universal, flat-rate pensions, corresponding with a classical Social Democratic notion of citizenship. But in welfare regime terms (Esping-Andersen, 1990), the Swedish welfare state in this field would seem to have moved increasingly towards a Conservative model, whereas the Danish welfare state has moved towards the Liberal pole. In alternative policy sector terms (Myles & Pierson, 2001), after two path-breaking reforms in 1959 and 1994/98/2001, respectively, Sweden has ended up with an earnings-related social insurance system whereas Denmark has ended up with a multi-pillar system.

Both the Danish and the Sweden pension systems seem economically sustainable in the future, but at least in the Danish case, the issue of sustainability was far from the only motive behind the changes, and even though the pension system that came into being is quite close to e.g. World Bank (1994) recommendations, there is nothing to indicate that recommendations from such international think tanks has played any role. This paper explores the mechanisms of path dependency and the highly different policy processes behind this divergence, and it ends up with a brief discussion of whether the pension systems may nevertheless produce functionally equivalent outcomes in the future, and whether the label 'Social Democratic welfare model' is at all relevant anymore.

The first part of the story would seem to confirm one of Esping-Andersen's (1990) hypotheses, namely that flat-rate universalism in the field of pensions is politically unsustainable in the long run. Both in Denmark and Sweden, means-tested old-age pensions had gradually developed into universal, flat-rate pensions, introduced in Sweden already in 1948, and in Denmark in two reforms in 1956 and 1964, respectively, the first introducing universal but means-tested pensions, the second one introducing full and equal pensions for everybody from the age of 67 (fully implemented by 1970). Formally, these systems might be labelled 'Beveridgean' basic security models but essentially, this is misleading. In the first place, the Scandinavian ideas of flat-rate universalism were much older - and so were the pensions systems: The first pension reform in Denmark stems from 1891, only a couple of years after Bismarck's first pension reform; it deliberately chose another path than Bismarck, and it came to inspire the reforms in New Zealand and some Australian states a few years later (Overbye, 1997). Secondly, as we shall see, the level of ambition in Scandinavian flat-rate universalism was much above the minimum protection recommended by Beveridge.

However, Esping-Andersen (1990) and Korpi & Palme (1998) have suggested that even the most generous flat-rate pension system becomes *politically* unsustainable in the long run as it is not be able to satisfy the needs of the upper middle classes for adequate income replacement after retirement. This will inevitably 'crowd in' private pensions, i.e. it will generate a mechanism of path dependency towards dualism where all citizens are no longer covered by a common system building on principles of solidarity. Allegedly, and echoing Titmuss' classical statement that 'welfare for the poor' inevitably becomes 'poor welfare', the better-off come to rely mainly on private arrangements and will lose commitment, perhaps even willingness to pay, to the public system (Korpi & Palme, 1998; Korpi, 2002). From a classical Social Democratic perspective, a 'multi-pillar' pension system is a *residual* or *recommodifying* one. Within this perspective, the introduction of an earnings-related component in the *public* pensions system in order to provide adequate income replacement for everybody and crowd out private arrangements for the middle classes, is interpreted as an effect of 'resource mobilisation', i.e. of the political strength of the Social Democratic party and the Labour Movement in general.

It can be noticed that this interpretation involves a conception of 'path dependency' which is far more dynamic than most interpretations of the concept; in fact, it even predicts that path dependency will automatically lead to 'path breaking'. Next, it emphasizes *political* factors rather than economic sustainability as the dynamic of change, unlike most current theories about the welfare state where economic 'challenges' are seen as the main dynamic, whereas politics is perceived more in terms of 'veto points' blocking change.

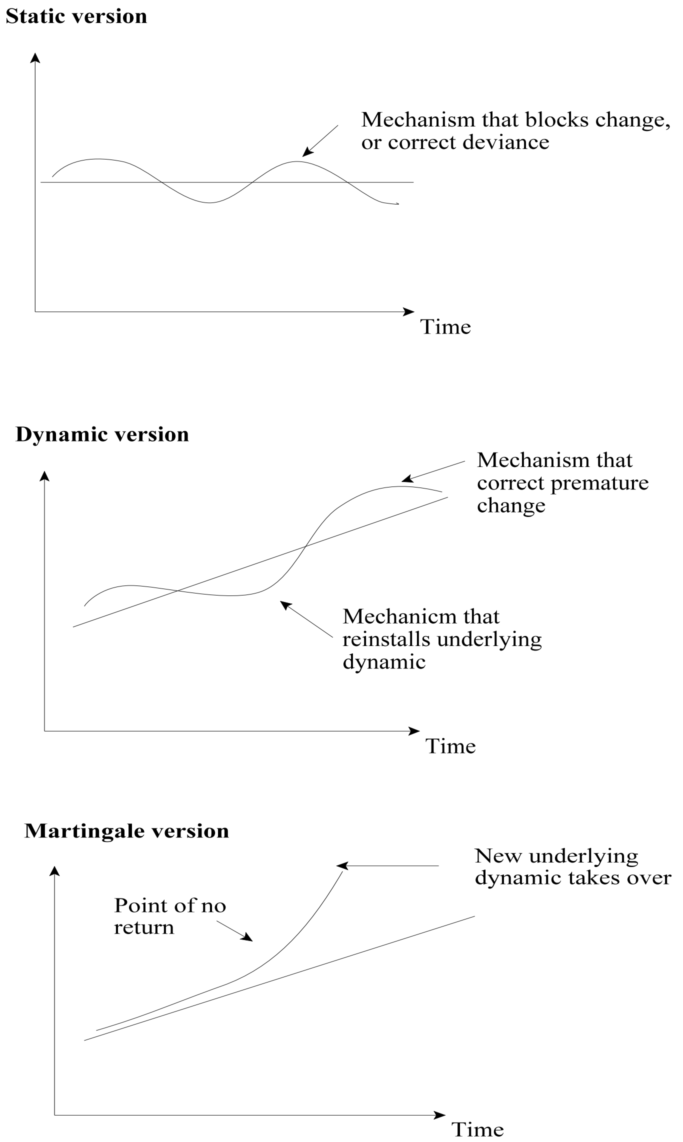
If it is correct to classify Sweden as a 'social insurance system', it seems that even the Swedish earnings-related version of universalism was not sustainable. Below, we shall examine what were the mechanisms of change in the two countries (although with main emphasis on Denmark), including a description of the highly different 'policy styles' behind the changes, in both cases with the aim of drawing some more general lessons about the sources of change of welfare systems and the mechanisms of path dependency. Finally, we shall also briefly discuss to what extent the formally very different pension systems that have come into being in the two countries may nevertheless produce equivalent results, as far as policy outcomes are concerned. Both from an analytical perspective, and from the perspective of policy prescription, this appears to be perhaps the most central issue.

2. Three types of path dependent change

The Swedish reforms essentially represent two instances of path breaking change, although it may be debated how radical these changes were. Denmark, on the other hand, represents an odd instance of continuity or path dependency which nevertheless brought at least as radical change as in Sweden - even though at the time of writing, this is hardly recognized by the Danish public.

This leads to some introductory comments on the notion of path dependency. At least three different versions may be distinguished. The first is the *static version* of path dependency (Figure 1). This is the notion of path dependency that is implicit in much of the 'veto point' literature and in many other contributions of the comparative welfare state literature of the 1990's. Welfare institutions are considered immovable or at least very difficult to change. If policy for whatever reason comes temporarily to deviate from the once established pattern, some mechanism - acting as a thermostat - that blocks change or corrects deviance will almost immediately come into action, bringing policy back to where it was; this may be interest associations, voter resistance or other mechanisms; welfare institutions don't change, except in path-breaking reforms with major conflict.

Figure 1. Three models of path dependency.



The next version is a *dynamic* one which is somewhat more in line with Pierson's (2000) notion of path dependency. Here, the underlying trend is not a static but rather a dynamic process such as the trend towards more and more universal welfare arrangements (or decommodification) up till the early 1980's in most European welfare states, in particular the Scandinavian ones. Another example could be the trend towards ever higher coverage with public day-care, once installed, in the Scandinavian countries. Here, there will be some mechanisms that reiterates the underlying dynamic if it suffers a temporary slow-down or backlash - and some mechanisms that correct premature change.

Finally, however, we also find in the literature a *martingale* notion of path dependency, notably in the article by March & Olsen (1984) where they coined the label of 'new institutionalism'. However, this is also the notion referred to by Korpi (2002) and Esping-Andersen (1990) when discussing what will happen to a universal flat-rate pension system if it is not reformed. The basic idea is that some small change which may for long go unnoticed gradually accumulates so that beyond a point of no return which is not always recognized, it becomes both irreversible and self-reinforcing, with the result that a new underlying dynamic is taking over. This may happen, e.g. if private or occupational pensions grows beyond a certain point. To a large extent, this seems to be what happened in Denmark, whereas in New Zealand, a similar process was deliberately broken off just a little before the point of no return (Overbye, 1997).

3. Whatever happened?

The story of pension reforms in Sweden is basically quite well-known. It includes two major reforms and some adjustments; here, we shall concentrate only on the major reforms. The first reform, passed in 1959 by an absolute minimum winning coalition of one vote, after a consultative referendum and an election, was the introduction of earnings-related pension supplements (ATP). It came to be seen as the 'crown jewel' of Swedish pension policy as it organised the middle classes into the common, public pension system, thus tending to crowd out private pensions. It was basically a pay-as-you-go system but included the building of a central fund during the first twenty years when contributions exceeded pension payments (actually this central fund was the main cause of opposition from the liberal and conservative parties). The scheme was highly redistributive as it was financed by proportional taxes without any ceilings whereas there was a ceiling on pension payments. Eventually, the scheme became even more redistributive as the ceiling was indexed by prices rather than wages, and in particular with the introduction of pension supplements for low income earners (introduced by 1967 and gradually increasing). Even though by 1994, 79 per cent received at least some earnings related pensions supplement (Green-Petersen & Lindbom, 2002), this meant that the Swedish system gradually became less earnings-related and less attractive for people with higher incomes.

If this was one of the *political* motives (of the bourgeois parties) behind the second big change of the Swedish pension system, decided in principle in 1994, with detailed legislation mainly being passed in 1998 and 2001 (in force as from 1999/2000), the other and far most important force was of course concern for *economic* sustainability in the future. The reform changed the system thoroughly from a defined-benefit scheme (based on 60 per cent of incomes during the best 15 years and minimum 30 years of work to obtain full benefits) to a defined-contribution scheme, fixing contributions at 16 + 2.5 per cent, the last part being an obligatory, individualised and fully funded private pillar. Rather than being an add-on to the basic pension, the contribution-related part now forms the backbone of the system, with a generous minimum guarantee pension filling the gap for those with low life incomes. A long transition period of nearly 20 years, quite different and not too transparent effects on different groups of employees, a strong crisis awareness in the Swedish population as well as among politicians, and the possibility to have the accumulated public fund help finance the transition costs, all contributed to the successful adoption of the reform. Around 1990 it also became highly visible that expenditures exceeded contributions, and that the state pension fund (AP) which still remained able to cover the deficit out of its incomes without raising taxes, would gradually be emptied over a couple of decades if nothing was done.

The changes of the Danish pension system have been much more chaotic or at least less planned and more incremental. Whereas the new Swedish pension reform was based on 10 years commission work, Denmark had three commissions (1964-67, 1973-77 and 1988) whose work did not result in any legislation; it had quite some legislation without commissioning; and the most important change was actually implemented without any legislation.

However, in the 1960's and 1970's, Denmark deliberately chose to expand its universal, flat-rate pension system to a Rolls-Royce version. Like in Sweden, the point of departure was a universal, flat-rate old age pension for everybody, decided in 1964 and fully implemented by 1970. As the 1964 reform was mainly to the benefit of people with high incomes, a minor, income-tested pensions supplement of some 20 per cent of basic pensions was introduced alongside the reform; however, this supplement was received by a large majority of pensioners. At the same time, there were special rules applying to public employees receiving state pension.

Unlike Sweden, and almost by accident, Norway (Overbye, 2001)[1], Denmark failed to introduce

[1] Overbye (2001) presents the story about Norway in terms of chaos theory: Because of a mine accident in the distant arctic island Svalbard in 1962, the Social Democratic government was overthrown by a vote of disconfidence in Parliament. Speculating about how to regain political power, the party then

an earnings-related component in the public pension system in the 1960's, even though the Social Democrats were in office 1957-1968. Instead, a rather small, employment-related but not earnings-related pension supplement (ATP), paid jointly by employers and employees, was added to the people's pension system by 1964, not least as compensation for an income political intervention in 1963. Later on, contributions were raised, and the ATP was extended also to the unemployed (even with double contributions) in order to ensure that they did not suffer too much loss in pension rights in addition to the loss of employment.

The explanation why Denmark did not follow the Swedish model is partly a story of having passed a window of opportunity, but this does not explain why no action was taken. In much welfare state literature, this is explained in terms of power resources, i.e. by the lower strength of the Danish labour movement. However, there are more plausible explanations. First and foremost, there were disagreement and ambivalent preferences within the labour movement. Several unions and their members, not least among the unskilled, thought that earnings-related pensions would break with the principle of equality and preferred to maintain and expand a flat-rate pension system (Rasmussen, 1996). It seems that even the Social Democratic leadership had uncertain preferences. In 1964, a commission of experts and bureaucrats (in 1965 supplemented by representatives of the parties) was appointed to consider possibilities but not to come up with a concrete proposal. In 1967, shortly before the Social Democratic government was overturned, and again in 1969, the Social Democrats half-heartedly presented a sketch which was refused by the other parties. It is quite remarkable that the conservative and liberal parties exploited the social democratic disagreement tactically, arguing that an earnings-related pension system would be unjust as it would increase inequality among pensioners.

Another explanation of the inaction was that the Danish flat-rate pensions were higher than those in the other Nordic countries; therefore, the need for supplements was lower. It may also have played a role that throughout the second half of the 20th century, a pay-as-you-go earnings-related scheme was never considered by any party or any commission. For reasons that are anything but obvious, only funded schemes were on the agenda, and not surprisingly, the standard argument against such a scheme was of course the double payment problem.

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looked to Sweden where the introduction of earnings-related pension supplements had divided the Swedish bourgeois parties. It then presented a reform proposal going in the same direction, hoping to introduce a similar conflict between the non-socialist parties in Norway. However, these parties were well aware of the problems of their Swedish sister parties and almost immediately agreed to promise to support such a proposal. Consequently, a reform akin to the Swedish, only somewhat modified, was proposed and passed by a *bourgeois* government in 1966.

Nevertheless, by 1970, a Social Pension Fund was formally established by a centre-right coalition government (1968-71) to finance future improvements of pensions. It was financed by an ear-marked tax of one, later on two, per cent of gross incomes, until contributions were abolished in 1982. It was never specified, however, which kind of pension improvements should be financed by the fund, and in effect, virtually no money was ever spent, as a pension reform was postponed in the 1970's, due to the economic crisis. Obviously, the establishment of the Social Pension Fund served mainly to legitimize a fiscal policy intervention aimed to reduce private consumption and to compensate for the lack of private savings, in order to limit the balance of payment problem. In the 1980's, the Fund was almost forgotten, and not too surprisingly, it was eventually confiscated by the Social Democratic government in 1999 (Law no. L114, dec.1998), arguing that numerous improvements for pensioners had already been adopted.

To some extent, the government was right. Throughout the 1970's, and to some extent even the 1980's, Denmark had continued along the path of universalism to build an ever more generous version of the flat-rate pension system, and with some justification, Danish scholars frequently considered the Danish system to be more 'Social Democratic' than its Swedish counterpart (Andersen, 1991). Pensioners were exempted from or compensated for all sorts of fiscal tightening and other crisis interventions. Unlike wage earners, pensioners enjoyed continuous improvements of real incomes throughout the period. When a Commission was finally set up by the government and the social partners in 1988 to elucidate the possibilities of introducing a labour market pension, it turned out that for low-wage single pensioners, the effective compensation rate was frequently around 100 per cent. The combination of special tax rules for single pensioners, generous housing allowances for tenants and tax reduction for homeowners, support for heating of dwellings, personal supplements, 50 per cent rebate on public transportation and a number of other special arrangements for pensioners meant that the effective minimum level of support was very high (Arbejdsmarkedspensionskommissionen, 1988).[2] According to the conventional 50 per cent median equivalence income criterion, poverty among pensioners was virtually non-existing (European Commission, 1995; Petersen, 1999; Förster, 2000).

However, while this system largely provided adequate support for single unskilled workers to maintain their former standard of living, it did not provide adequate income replacement for the higher middle classes, and simultaneously with the improvement of basic support for pensioners, funds-based private or occupational pensions expanded. Still, this seems to have happened more

2 Furthermore, medical treatment (except medicine) is free in Denmark, and in 1990, pensioners were also granted free home help.

because of initiatives from above than because of pressures from below. A high age of retirement, and in particular a very high rate of home ownership meant that the opportunities to maintain a decent level of living for the middle classes were not all that bad. But the state desperately wanted to stimulate any sort of savings; besides, former state pensions to public employees was increasingly converted to occupational pensions.

The exemption of pensions savings from taxation, along with high marginal tax rates, reaching a peak of 73 per cent in the early 1980's, gave a strong incentive to private and occupational pensions (by 2002, however, tax subsidization of private and occupational pensions is rather small)[3]. And partly because of a dramatic expansion of public sector employment, partly because occupational pensions among public employees spread downwards, this contributed significantly to the expansion of occupational pensions. In all, this meant that by the early 1980's, a dual pension system had in effect developed, where a majority of pensioners had to rely on basic pensions only whereas a big minority had supplementary occupational or private pensions. The coverage by occupational and private pensions was somewhat uncertain. According to one estimate (Vestero-Jensen, 1985), about 39 per cent had an occupational pension, and 59 per cent some private pensions savings. According to another estimate, based on surveys, coverage by occupational pensions was only about one-fourth (Blindekilde et al., 2002). But whatever may be the true figure, the development had passed the point of no return. To introduce an earnings-related public pension at this stage would be difficult. Even though it involved a very strong 'double payment' problem, it would be far less complicated, politically and administratively, to expand along the path of occupational pensions.

And this was considered necessary and desirable by labour movement leaders (in particular by the unions). By 1984, long before OECD, the World Bank and others entered the ageing crisis business, a (temporary) decline of fertility rates to 1.4 and prognoses about a significant decline in the population until 2025[4] generated quite some concern about the 'pension bomb' and the future of the pension system. Thus, the nationwide association of unions (LO) regarded it necessary to build up a labour market pension system as the only feasible way to obtain future improvements, or perhaps even partly as an alternative to the basic pension which was feared to be unsustainable in the long run. Not less importantly, the unions had lost the struggle for

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3 There remains a subsidy (Government, 2000), as pensioners will frequently have lower tax rates than those who are economically active. But the difference is rather small, and annual capital gains and interest of pension funds are taxed by 15 per cent.

4 In the population prognosis of 1984, the population in the year 2025 was estimated to around 4.2 million, as compared to about 5.1 million in 1984. By 2002, the estimate is about 5.8 million.

'economic democracy' and had to give up their ambition to build a central fund controlled by the unions; building of pension funds seemed an attractive, second best alternative.[5] LO presented a proposal for an integrated reform with obligatory labour market pensions in 1985, but in spite of government support for the idea of a labour market pension, from some of the most centrist conservative ministers even for an obligatory arrangement, nothing happened until 1988 when the issue could be linked to an urgent need to reduce the balance of payment deficit.

In 1988, a tripartite labour market pension commission was set up to explore the possibilities of introducing an supplementary occupational pension system. Actually, the commission report in December the same year documented that all welfare arrangements for pensioners taken into consideration, coverage for low-income groups was far better than commonly believed. Politically, however, the commission report had only little direct influence on subsequent events. In his 1989 new years speech, the Conservative prime minister denounced the idea of an obligatory labour market pension and, in accordance with the employers' demands, left it to the social partners to negotiate pension improvements as part of collective agreements. Later in 1989, the increasingly rightist government failed to reach agreement with the Social Democrats on a big crisis package including a labour market pension. But in the autumn 1989, the centrist Conservative minister of finance and the association of Danish municipalities negotiated a (small) labour market pension for most public employees not yet covered. In 1991, the Danish LO, including not least the Metalworkers' union, had lost patience and gave up the idea of an obligatory arrangement by law and negotiated a labour market pension with the employers' association, and in the following years, a labour market pension was included in nearly all collective agreements - after substantial efforts by the union leadership to persuade reluctant rank and file members, not least among the unskilled. In 2001, the target for the large majority of the new pensions arrangements was set to 9 per cent by 2004 (3 per cent paid by the employees, 6 per cent by the employers, as originally proposed by LO in 1985), as compared to some 12-17 per cent for most of the already existing labour market pension agreements. Thereby the unions disconfirmed the conventional wisdom that the double payment problem would make such a manoeuvre impossible.

The introduction of labour market pensions did not complete the story about pension reforms, however. In 1990, a new indexation of pensions and other transfer incomes was introduced (in

5 The unions did obtain a large, union-controlled fund (LD-Lønmodtagernes Dyrtidsfond) in 1979 when wage increases due to price indexation were frozen in a pensions savings fund which has grown big but will be emptied around 2020. Unlike this fund and the already existing pension funds, the new pensions funds are controlled jointly by representatives from unions and employers' associations.

agreement between nearly all parties), linking them to wages rather than prices (mainly because of declining real wages at the time) but at the same time exempting the component of wage increases devoted to pensions improvements. Alongside a slight manipulation by the Ministry of Finance, using fixed rather than variable weights in the computation of wage increases in order not to incorporate the effect of changes in the occupational structure, this introduced a slow-long term lag in the regulation of transfers.

Thus, already in the 1990's, (basic) pension expenditure began to decline quite markedly, relative to the total economy, and by 2000, relative spending was even below the 1972 level, in spite of an increase in the number of old-age pensioners by one-third (Table 1). From 1972/73 to a peak level in 1981, pensions increased more than the economy in general. The total economic product is measured conservatively here by Gross Factor Income (GFI). This measure does not include indirect taxes which have increased relatively over the period - and which have to be paid also by pensioners. In the 1980's, relative expenditures on pensions declined slightly, and from 1994, alongside renewed growth in the economy, public expenditures on basic pensions even went well below the 1972 level. Thus, even before the labour market pensions and other reforms began to have an effect, there were no short-term economic pressures for retrenchment in the field of pensions, and even in the long run, the problem would not so much be pension expenditures but rather insufficient tax revenues from a small labour force and possibly increased spending for health care and home help. However, as can also be seen from Table 1, even health care spending have not gone out of control so far, and during the 1990's, total government outlays has declined very rapidly in relation to the economy - more than usually recognized, because of the tax reform in 1993/94 which artificially increased government spending by making nearly all remaining non-taxed transfers fully taxable income.

Table 1. Public expenditures on basic old age pensions, health care, and total government outlays, as per cent of Gross Factor Income (GFI), 1972-2000.[1)]

	basic old age pensions	health care	total gov. outlays
1972/73	5.6*	6.3	...
1981	6.5*	7.0	...
1992	5.9*	6.2	69.0*
1993	6.0*	6.4	72.1*
1994	6.0	6.2	70.5
1995	5.9	6.0	69.0
1996	5.7	6.1	68.7
1997	5.4	6.0	66.9
1998	5.3	6.1	66.1
1999	5.1	6.1	64.0
2000	4.9	5.9	61.1
Change 1993-2000	-1.1	-0.5	-11.0

1) Old age pensions does not include state pensions for civil servants of the state and municipalities, nor does it include payment from the funds-based ATP scheme. That is, only basic pensions (basic amount plus pension supplements and individual support) is included.

*) Basic old age pension 1972-1993 corrected for tax reform in 1994, based on the conservative assumption that the proportion of GFI spent on basic old-age pensions was constant from 1993 to 1994 (for a similar estimate, see Ministry of Finance, 1995: 36). This involves an upward correction of pre-1993 fiures by 1,1 percentage points. Pre-1988 figures are corrected from old to new national account system based on the experiences from 1990-93 where data are available for both; this means a downward adjustment of pre-1993 figures by approximately 0.2 per cent of GFI. Figures are *not* corrected for transfer of 'pre-retirement old age pensioners' and widow pensioners to disablement pensioners from 1983/1984. Based on a comparison of disablement pensioners' and old-age pensioners' share of GFI 1983-1984, this may lead to an over-estimation of pre-1984 figures by 0.3 - 0.4 per cent. This means that the decline in the 1980's is somewhat exaggerated but does not affect the overall conclusion.

Total government outlays 1992-1993 is corrected for 'grossification' of transfers in 1994 as above. This means an upgrading by 1.9 per cent of GFI in both years, corresponding to the increase in gross expenditures necessary to neutralise the 'grossification'. All informations based on new 1995 national account system.

Health care expenditures 1972-1992 excludes administration and are based on old national account system as this yeilds exactly the same figures for 1990-1992 for expenditures including administration, calculated on the basis of the new national account system. Expenditures 1993-2000 are based on new national account system and include administration.

1997-2000 figures are preliminary, as published by June, 2001.

Sources: Own calculations, based on S.E. and St-10., several iss., and Andersen & Christiansen (1991).

However, a number of reforms will de jure or de facto make basic pensions more targeted towards the less wealthy in the future, or they have already done so. In 1983, the principle of basic pensions for everybody over the age of 67 was violated when it became tested against occupational income for the 67-69 years old; in 1994, this was extended to all old-age pensioners, regardless of age (Ploug, 2001). Although in practical terms, this meant very little and was motivated solely by the need to find small savings on the state budget, it demonstrated that even the basic amount component of the basic old-age pension was not sacred. More importantly, however, the income-tested pensions supplement component of the basic pension was increased substantially as part of the 1993 tax reform (implemented in 1994). This could be justified mainly as a technical adjustment: Alongside the tax reform, most transfers including pensions came to be paid as fully taxable income and were increased accordingly. Partly as an adjustment to this, the pensions supplement component of basic pensions was expanded but at the same time, the balance between the two components was radically changed. This has continued little by little, and in 2002, income-tested pension supplements for the first time exceeded the basic amount paid to everybody. Undoubtedly, this was done deliberately as an obfuscation of long-term retrenchment. But it was partly a technical correction, and at the same time, the income testing became more lenient so that in the short run, a smaller proportion than previously had their pensions supplements reduced.

None the less, since the mid-1990's, the proportion with reduced pensions supplements has been steadily increasing, along with the increasing number of new pensioners having a supplementary pension. Besides, yet another pensions savings scheme was introduced from 1998: The ‘temporary pensions saving’. This was introduced as a means to prevent over-heating of the economy but made permanent from 1999 under the label ‘the special pensions saving’ (SP). This scheme is consisting of a one-percent fee levied on all income and is scheduled to be paid back over a ten-year period after retirement. In 1999, the scheme was changed from a earnings-related to a flat-rate pensions saving (like the ATP) but by 2002, the newly elected bourgeois government (with surprisingly little public attention) changed it back (with effect from 2001) so that it no longer contains any redistribution.

Figure 2. The Danish Multipillar Pension System, by 2002.

1.	Special support for pensioners	* (Discretionary) personal supplements for pensioners with a difficult economic situation (only for particular expenditures, e.g. for glasses), and (means-tested) health supplements. * General support arrangements for pensioners - higher housing allowances, lower real estate taxes - heating (means tested) - rebates (e.g. 50 % on public transportation)
2.	Basic Pension	A. Basic amount: Flat-rate for (nearly) all. 1) B. Pensions supplements: Income tested 1)
3.	Supplementary, fully funded public pension	A. ATP (1964) Wage earners, employment-related only.2) B. SP (1998) contribution 1 % of all incomes, strictly actuarial. 3)
4.	Occupational Pensions4)	From 1993 included in nearly all collective agreements, from 2004 contributions typically 9-17 per cent (two thirds of which is paid by employer). Numerous funds. Some regulation of investments, but not of risk sharing.
5.	Private Pensions4)	

1) By 2002, basic pension is evenly divided between basic amount and pensions supplement (about 7070 and 7110 annually for a single pensioner, respectively).

2) ATP='Ordinary Supplementary Pension'. By 2002, contribution for privately employed is about 360 , two thirds of which is paid by the employer. For unemployed, it is twice as high. For some groups of public employees, it is only about one-half, depending on collective agreements. Full-time contribution is paid for everybody working more than 27 hours, i.e. nearly all part-time employed.

3) SP='Special Pensions Savings'. 1999-2000, savings were flat-rate, i.e. the SP was highly redistributive.

4) Tax subsidies to private and occupational pensions savings have become quite small during the 1980's and 1990's.

This programme adds yet another element to supplementary pensions that will reduce the state's unfunded pension spending in the future. Indeed, the basic pension will play a more and more limited role, as the new pension arrangements mature. According to an estimation by the Danish Economic Council from 1998, shortly after the introduction of the SP scheme, basic pensions is estimated to provide only 30 per cent of total incomes from collective pension arrangements by 2045 when the system has fully maturated. The upper half among the pensioners are estimated to receive no pension supplements at all, that is, they will receive only the basic amount (of some 7.050 annually, in 2002 prices). Funded public arrangements (flat-rate ATP and earnings-related SP) are expected to provide 21 per cent, and the rest - 49 per cent - is provided by labour market pensions.[6] In other words, apart from fully funded arrangements, the state's responsibility for proving incomes for pensioners will be more limited than in almost any other rich country. Furthermore, this is based on the assumption that all arrangements remain unchanged. For political (rather than economic) reasons, this is not too likely: Even basic pensions for the better-off are quite likely to be abolished (see below).

Table 2. Prognosis about composition of Danish pensioners' incomes from collective pensions arrangements, 2045. By income deciles. Based on 2002 arrangements. Percentages.

	D1	D2	D3	D4	D5	D6	D7	D8	D9	D10	All
Basic amount	69	52	42	37	33	29	24	20	17	11	25
Pens.supplem.	30	23	17	12	5	0	0	0	0	0	5
Basic pension, total	99	75	59	49	38	29	24	20	17	11	30
ATP+SP	1	23	37	40	33	29	24	20	16	10	21
Labour market pens.	0	2	4	11	29	42	52	60	67	79	49
Total	100	100	100	100	100	100	100	100	100	100	100

Not including private pensions and other savings. Based on assumption of increase of labour market pensions contributions to 9 per cent from 2010 (estimations are for the 65-69 years old). Based on rather crude assumptions concerning mobility (see footnote 5).
Source: Economic Council (1998: 154-56).

Whether or not the Danish system will be subject to further changes, it is obvious that a very dramatic change has taken place, actually by an incremental process without any big reforms regarded as path-breaking. Only the new labour market pensions from the early 1990's might qualify for this label, but they were not really recognized as such: rather, it was perceived as an add-on to the existing pensions.

3. Some general lessons: Pensions policy

The experiences from the Danish and Swedish pension reforms have some quite important theoretical corollaries. In the first place, *as far as policy substance is concerned*, we can note that:

Flat-rate universalism in the field of pensions is economically quite sound but politically

6 The calculation are based on too crude assumptions regarding mortality and occupational mobility between the employed and unemployed. A similar but more refined calculation by the Government (2000:85) estimates that basic pensions will provide 39 per cent (detailed figures are not published, however).

vulnerable as it tends to crowd in occupational and other private pension arrangements. However, the main source of change was not pressure from below but rather initiatives from above. Besides, the Swedish earnings-related universalism appeared equally unstable as it has been transformed into a quite Bismarckian or merit-based system - although an encompassing one that maintains important traits of universalism.

It is possible, as in both Denmark and Sweden, to avert the old age crisis effectively by big reforms that are considered legitimate by the population.

It is possible, as in Sweden, to transform a defined benefit scheme completely into a defined contribution scheme (if the period of transition is sufficiently long, and if opposition parties have weak incentives to mobilise against it).

It is possible, as in Denmark, to build a new, fully funded pension scheme alongside the maintenance of the pay-as-you-go scheme, in spite of the double payment problem.

This does not mean that political obstacles are easy to overcome. But it does mean that they are not insurmountable. Whether these reforms have cured the illness but killed the patient, that is, whether these reforms have more or less dismantled the universalist welfare state, will be discussed below.

4. Path dependency and causes of change

Next, as far as *causes of change is concerned*, the Danish case to quite some extent challenge the widespread assumption that economic challenges are the main source of welfare state change - the perspective of necessary reforms facing political resistance - unlike in the past where (class) interests were considered the main dynamic. Obviously, *perceptions* of economic challenges have played a role, not least for the government and for the economic policy elites.

But objectively speaking, and not least judged from a comparative perspective, it is difficult to claim that the Danish pension system of the 1980's was unsustainable (as indicated by relatively declining public expenditures for old-age pensions in the 1990's - although, admittedly, this was a special situation). However, as noted by Myles and Pierson (2001), there is no straightforward relationship between ‘objective’ and perceived economic challenges in this field: Concern for the ‘ageing crisis’ often seems equally strong in countries with pension systems (or age structures) which do not appear threatening to the welfare state. Next, it seems obvious that other motives also determined the behaviour of trade union elites who were core actors behind the most radical change, i.e. the introduction of a general labour market pension. Such motives explicitly included the wish to obtain access to what was considered a fringe benefit of those wage earner groups higher up the ladder. And they certainly also include a wish to obtain control over big economic funds, not least among the professional trade union elite. Undoubtedly, they acted out of perceived collective interests. But self-interests of the trade union leadership and professionals seems at least as obvious.[7] In short, economic sustainability should not be considered the only source of change - and not even *perceptions* of economic sustainability (which need to be explained) are the only motives. (Perceptions of) political interests appear equally important.

The Danish and Swedish experience also have important corollaries for the debate about path dependency. In both countries, it is no exaggeration to speak of path-breaking change. At the same time, these reforms were highly path dependent. In the Swedish case, this is hardly surprising. Even path-breaking reforms always build on an institutional legacy which influence strongly on the direction of the reform. However, the Danish case is more theoretically challenging. Following the predictions of Esping-Andersen (1990), but partly driven by other forces[8], the wish to maintain the flat-rate people's pensions system almost inevitably generated a new path in quite another direction which will in the long run reduce the role of the public pension system very significantly, perhaps even into a support system mainly for the poor - nearly the opposite of what was originally intended. And it is difficult to point out what was the point of no return. But obviously, small, incremental changes started to generate a logic or a dynamic of their own, i.e. simply a new path, even though nobody ever realized the moment of path breaking. Suddenly actors found themselves on their way on a new path.

This may of course be of little theoretical significance if it is only a Danish peculiarity. However, even if the Danish case may be extreme, it seems more than a peculiarity. It illustrates a situation where some initial small changes, introduced for various (often short-term) reasons, and not as part of a pre-designed plan, at some point become self-reinforcing and introduce another logic. Until the 1980's, nobody really envisaged what would happen, and until the mid-1990's, only a few people realised what had in effect already happened long time ago (Cox, 1997). Even at the time of writing, it is the general perception among the Danish public that the pension system will have to change in the future - not that it has already done so.

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7 It may be added that the behaviour of the professional investors of the pension funds have by no means come close to what bourgeois opponents of economic democracy feared in the 1970's. Rather, on a number of occasions, the pension funds often appear to have given one-sided emphasis to 'shareholder value' rather than to 'stakeholder value'.

8 As mentioned, the changes do not seem much influenced by any strong demand from below. And one may speculate whether young people at all care about their future as pensioners; it could be suggested that until their 40's, this is probably a too distant future for most people to care about at all.

5. Policy style

This 'martingale' notion of path dependency is related to what may be labelled policy style. The Danish and Swedish policy processes represent two very different policy styles. We may have exaggerated the rationality of policy change in Sweden, characterised to a large extent by a rational problem-solving approach, combined, of course, with negotiations and compromise between actors with relatively clear preferences. But the difference to Denmark is quite obvious. The Danish policy style comes more close to what Cohen, March and Olsen (1972) labelled a 'garbage can model' where different actors, different problems, and different solutions are mixed together in a somewhat chaotic manner, and where the temporal coincidence is at least as important as the logical one. However, a better model of the Danish decision making style is perhaps the model of incrementalism - the 'muddling through'-model suggested already in the late 1950's by Charles Lindblom (1959).

Here we do not consider the normative aspects about what kind of political decision making process is advisable. Rather, we emphasize the description of a decision-making process where actors have rather uncertain long-term goals but relatively clear short-term preferences, determined by the situation as it stands. In the Danish case, it is obvious that both short-term tactical goals and short-term fiscal considerations played a major role. The introduction of ATP in 1964 was directly related to the government's intervention in collective agreements one year earlier; the stimulus to private and occupational pensions savings in the 1970's originated to a large extent in a desperate wish to limit private consumption (often referred to as the 'achilles heel' of the Danish economy, due to the chronic balance of payment deficit); the introduction of large-scale occupational pensions was welcomed by a bourgeois government as a means to cooperate with the trade unions, and even more as a means to increase savings and solve the balance of payment-problem; finally, the SP introduced in 1998 was apparently intended only as a temporary measure to reduce private consumption that year.

Until the mid-1990's, it appears that nobody had any 'master plan', but neither was the outcome totally unpredictable. On the basis of decisions made at one point of time, one could to quite some extent stipulate the problem perceptions, the short-term preferences, and the most likely solutions at a later point of time. We shall not develop this further at this stage. But it does appear to be a promising field to search for a new formulation of the notion of path dependency. Partly because of different combinations of weak/strong governments and weak/strong parliaments, partly for other reasons which may be summarized as 'political tradition', different countries have different policy styles. But polities characterised by incrementalism can be equally dynamic as polities adopting a rational problem solving approach to political decision making.

6. Equivalent or different outcomes?

The notion of incrementalism may also help evaluating whether the Danish and Swedish pension systems, in spite of institutional differences, may produce similar or different outcomes in the future. Formally speaking, Sweden has maintained an encompassing, predominantly public pension system whereas the Danish system is gradually transformed into a multipillar system with a welfare mix where the public, flat-rate component will become only a minor part. Still, apart from concealing the figures on public expenditure (as labour market pension contributions are formally private expenditures), the Danish system might well produce equivalent outcomes. Pensions will be more earnings-related in Denmark, but this holds also for Sweden. Sweden provides a high minimum support, but so far, this holds also for Denmark, probably even more so (NOSOSCO, 2001). Furthermore, calculations by the Danish Government (2000) have indicated that taken together, the new pensions arrangements would contribute quite significantly to *increasing* equality among pensioners. Since then, the SP has been changed in 2002 from a highly redistributive to a neutral scheme (at best), but even with this change, the projections in terms of equality would probably be relatively positive if we assume that no changes are made in present arrangements.

However, the changes may have strong symbolic effects on the framing of pension issues in the future. Therefore, in the long run, the reforms may be more than 'just' a matter of 'welfare pluralism' or 'changing the welfare mix'. The emerging Danish pensions system is more likely than its Swedish counterpart to foster a logic of residualism which is already highly visible in the pensions debate. As occupational pensions mature, not only the pensions supplement component of the basic pension (2 B in Figure 2 above) is bound to decline. The process is likely to proceed further and to affect also the special support arrangements for pensioners, as the perception of pensioners as a 'weak group' that deserves 'special support' is likely to change. Discretionary, personal supplements have already been declining in recent years, and housing allowances were cut quite substantially in 1998 (but only for the better-off). In the long run, other special arrangements for pensioners are likely to be abolished as well. At best, they might be maintained but targeted to the weakest groups among pensioners. But equally likely, the effective minimum pension level (including special arrangements) will simply decline.

Further, it seems likely that following an ever stronger logic of residualism, even the basic amount that is presently given to nearly all old age pensioners may also come under pressure; it has already for some years been a popular target of attack for the youth associations of several political parties (although this is certainly premature), and in the future, many better-off pensioners will not even have very strong incentives to defend it. To repeat, this is not due to economic pressures on the welfare system, but to a logic of residualism being applied to the pensions system, according to which public money should not be allocated to those who can manage on their own. As public pensions rights (apart from the funds-based arrangements) are not related to contributions, and as public pensions for increasingly large groups are no longer essential means to live decently as citizens, the logic will almost inevitably change from citizenship or reciprocity to a logic of residualism. This leaves, in principle, two possibilities. The first is that public means simply become more targeted, so that minimum levels are maintained. However, this hinges exclusively on a solidarity of a quite altruistic nature. Furthermore, those most in need of support will be weak groups with limited ability to defend their rights. Even though 'welfare for the poor' may not inevitably lead to 'poor welfare', to quote Titmuss, it does seem likely that minimum standards, relatively speaking at least, will decline. In the long run, quite broad groups are likely to lose interest in the public system at best; at worst, they may even be less willing to pay.

Other directions are conceivable, of course. Trade unions may react when more and more people among their members begin to lose pensions supplements; they may argue that this was never intended, that their members have been cheated, and that means-testing should be more lenient so that labour market pensions remain a supplement rather than a replacement. With favourable economic conditions, this is not a completely unlikely scenario.[9] But at any rate, the assessment of change, including the question of functional equivalence between the Swedish and the Danish scheme, will have to include a consideration of the changing framing of the pensions issue, from a matter of citizenship rights, to a matter of individual achievement and residual welfare.

[9] Still, there is the chance that new political actors may change the picture: In 2002, the right-wing populist Danish People's Party which forms the parliamentary basis of the Liberal-Conservative coalition government, has demanded that personal supplements are reestablished on previous levels, and that the basic old-age pension is increased, at least for pensioners having no other incomes except ATP (the 'old' flat-rate labour market pension).

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