

Public Policy toward Employee Benefits in the United States, Canada and Taiwan: Lessons for European Integration

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Abstract. Most governments intervene in the labor market to promote the provision of certain merit goods such as retirement income and health insurance. As economic integration has progressed within the European Community, questions have arisen concerning the harmonization of such benefits. Using case studies from three non-EC countries — the U.S., Canada, and Taiwan — the authors show that benefit structures and decisions reflect institutions which are difficult to change and whose patterns do not seem to reflect a simple economic determinism.

The U.S. and Canada, two similar countries with integrated product markets, have adopted very different health insurance policies, but similar pension policies. Taiwan, despite its different stage of development, has a Canadian-style health insurance system and is currently grappling with how to arrange its pensions. A key outcome of the benefit-decision process is whether entitlements are external to the firm or contingent on maintaining a specific job attachment.

An important factor in modifying benefit arrangements is the degree of social concertation present in national political systems. Benefits systems are best designed or reformed when institutions permit discussion of macro pressures. EC countries, now considering harmonization of economic institutions, have the opportunity to modernize their benefit arrangements.

Since its inception in the late 1950s, the European community has been moving toward greater economic integration. Initially, such inte-

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gration was viewed as largely a matter of removing barriers to intra-community exports and imports. Gradually, however, the concept has widened to include more general economic coordination and harmonization of regulations and institutions. This broader concept now extends to labor-market institutions under the general heading of "Social Europe".

Labor-market institutions can vary widely from country to country. Although economists often prefer to view institutions as arising from efficiency considerations, the reality — as will be demonstrated by example below — is more complex. Harmonization of labor-market institutions at the micro (firm) level would be relatively simple if abstract efficiency were the only influence. Integration of product markets with the EC would give all firms the same incentives, and Adam Smith's "invisible hand" would guide them toward similar policies regarding compensation and other human resource practices. Even at the macro (national) level, a unified product market might be expected to lead governments to similar public policies regarding so-called "merit goods" linked to the labor market.

Governments around the world have taken a special role for themselves in promoting use of a variety of merit goods, such as basic education and housing. Certain public interventions, however, have been closely linked to the employment relationship. These include expanding provision of retirement income through public and private pensions and facilitating access to health insurance. Those two areas — pensions and health insurance — have been selected to illustrate the problems and options facing the EC regarding employment-linked merit goods. Is it likely that natural economic forces will produce a harmonization of such practices within the EC, based on integration of product markets? Using examples from three non-EC countries — the U.S., Canada, and Taiwan — this paper suggests the answer is "no".

It is concluded that while efficiency counts for something in the evolution of employment-related merit goods, history and institutional rigidity matter a great deal more, both at the micro and macro levels. To be sure, some policies are preferable to others, particularly in the face of shifts toward intensified product-market integration and competition. But an important determinant of whether countries can respond to such shifts is the degree of "social concertation" that characterizes their economies.

Within the EC, social concertation is often viewed as a corporatist mechanism by which employers, unions, and government representatives are brought together to discuss larger challenges facing their economies. Discrepancies between narrow micro interests and the

broad macro interest are reviewed and policies evolve with the macro-side taken into account. However, corporatism is not essential. The key element is the national ability to look at macro issues as more than a summing up of decentralized micro incentives. Such an ability might come through the political process rather than through corporatist dialogues among the "social partners". But where concertation is not possible — where public policy is largely based on a decentralized view — dysfunctional decisions may result.

I. A Three-Country Comparison

Three non-EC countries — the U.S., Canada, and Taiwan — have been chosen to illustrate the public policy and private policy options available to Europe as economic integration proceeds. The first two are economically-advanced countries with high standards of living, as Table 1 illustrates. Both countries have been each other's major trading partner and recently both have signed a free-trade agreement which should foster still more interdependence. The U.S. and Canada might be viewed as analogous to some of the higher-income countries within the EC. Taiwan, in contrast, is a rapidly-growing industrializing economy with a much lower absolute standard of living at present than the U.S. or Canada. Its growth has been export-oriented in the context of important trade linkages to the U.S. Taiwan might be viewed as analogous to the

Table 1. Selected Economic Indicators for Canada, the U.S., and Taiwan

	Canada	U.S.	Taiwan
Population in 1990 (millions)	27	250	20
Annual population growth rate, 1980-1990 (per cent)	0.9	0.9	1.4
Per capita GNP in US\$ (thousands)	\$22	\$22	\$8
Hourly compensation in 1990, manufacturing, in US\$	\$16.02	\$14.77	\$3.95
Unionization rate, members as % of total employment, 1990	32%	14%	33%
Trend in unionization rate, 1980-1990	Falling slowly	Large drop	Increasing rapidly

Source: U.S. Department of Labor, Bureau of International Labor Affairs, *Foreign Labor Trends*, various issues; *Survey of Current Business*, vol. 72 (January 1992), p. 20; *Employment and Earnings*, vol. 39 (January 1992), pp. 162, 228; U.S. Bureau of the Census, *Statistical Abstract of the United States, 1991* (Washington: GPO, 1991), p. 7; Bureau of National Affairs, Inc., *Daily Labor Report*, January 7, 1992, p. B3.

lower-income countries within the EC which hope to gain from open access to the markets of the higher-income center.

If economic determinism was the rule in establishing practices regarding pensions and health insurance, the U.S. and Canada might be expected to be very similar — if not identical — in what they provide. In contrast, both nations might be expected to be very different from Taiwan, a country at an earlier stage of development. Reality confounds such expectations, however.

The U.S. and Canada — despite their similar stages of development and their economic interdependency — have made quite different choices with regard to health insurance provision. But their choices have not been so different with regard to pensions. In general, Canada has been more willing to countenance government intervention in benefit provision than the U.S. Thus, ideology will be seen to play a key role in establishing employee benefit systems, with a *laissez-faire* philosophy more characteristic of the U.S. than of Canada. While both the U.S. and Canada have long institutional and ideological histories which have influenced their approaches to benefit provision, Taiwan — because of its rapidly increasing standard of living — is now at a stage where it must choose its approach. And, indeed, that process is under way. So far, Taiwan has chosen a Canadian-style approach to health insurance but is still pondering the direction it should move with regards to pensions.

The period in which such choices are made is an important influence on the choice outcome. When the choice “window” opens for a country, the ultimate decision reflects the winds prevailing in the economy and the prominent ideological tendencies at that time. Choices made years ago may reflect economic conditions and political sentiments of a bygone era. Thus, the U.S. tilt toward a private, decentralized benefit system reflected a conservative period of large-firm ascendancy and an associated idealized norm of worker attachments to the employer and job security. Taiwan, because it is making decisions now, is not locked into a system based on an outmoded model of the employment relationship.

EC countries — as a result of the process of economic integration in the 1990s — have the chance to re-open their choice windows, or at least to reexamine choices previously made. Economists have long believed that labor-market pressures are derived from the product market. If the product market is to become more competitive and uncertain, surely there are implications for the kinds of pension and health insurance arrangements that would be desirable for EC countries. It is argued below that such arrangements are best suited to

the kinds of labor mobility (voluntary and involuntary) that results from modern product-market pressures if they are *external* to the firm. “External” means that entitlements are not contingent on the employee remaining with a specific employer. The opening of the choice window for EC countries can allow modern market pressures to be reflected in benefit structures.

II. A Brief Overview of U.S. Employee Benefits¹

Prior to the 1930s, the U.S. relied primarily on private provision of benefits.² For most workers, this meant saving for retirement and/or relying on family support in old age. It meant paying on an out-of-pocket basis for medical care, especially since the concept of health insurance had not really evolved. Some large employers did have pensions plans, although these covered relatively few workers and often were unfunded or partially funded. Even the few covered workers might receive no pension in the end, since pensions were often not vested or required very long service before vesting. Health insurance through the employer was at most embryonic. Life insurance was sometimes available to employees, in part as a marketing tool for insurance carriers. Income tax treatment of such benefits was somewhat ambiguous. But since most workers did not pay income taxes, the tax code was a minor matter.

Some employers regarded their benefit offerings as good investments. They may have seen benefits as promoting employee “goodwill”, keeping out unions, or contributing to some other corporate goal. Other employers saw such “welfare work” (as it was revealingly termed), as an example of social uplift.³ They viewed welfare work paternally or as a “social responsibility” of business (as it might be termed today). Whatever business chose to do in the benefit area, however, was not in response to government policy since there was no government policy encouraging benefit provision by firms.

i. The Great Depression and American social security

The Great Depression of the 1930s marked a significant change in attitudes toward government intervention in the labor market in the U.S. Due to the depression, private company welfare systems often failed or were cut back. Thus, government provision was increasingly seen as an alternative, an ideological shift triggered by economic adver-

Table 2. Summary of Social Security and Leave Provisions: Canada, the U.S., and Taiwan

	Canada	U.S.	Taiwan
Initial date of program	1951	1935	1950
Pension element	Universal pension for all residents. A flat-rate tier covers all provinces. A second, earnings-related tier covers all except Quebec. (Quebec has an equivalent second tier.) Normal retirement age is 65.	Covers most employed persons with specified length of employment history. Some public workers not covered. Retirement benefit is earnings-related. Normal retirement age is 65.	Covers most employees in firms with five or more employees. Benefit paid is a lump sum related to work experience and past earnings. Normal retirement age is 60 for men; 55 for women.
Medical element	Virtually universal health insurance based on residence. Operated by provinces with federal subsidy.	Coverage for those insured by pension element who have attained 65 under Medicare. Means-tested program for indigents (Medicaid).	Coverage for those insured by pension element. Dependents not covered. Various medical, hospital and maternity benefits.
Financing of pension and medical elements	Primarily financed by general revenue from provincial and federal governments. Also payroll tax in Quebec and contributions by insured in some provinces.	Medicare financed by employer and employee payroll taxes with optional additional coverage paid by insured person. Medicaid financed by general revenue.	Primarily financed by employer and employee payroll taxes.
Family leaves	Provincial and federal requirements for unpaid maternity leave. Unemployment insurance benefits for maternity. Parental benefit (to parent of either sex).	A few states require employers to provide unpaid maternity or other family leave.	Under Labor Standards Law (covering about four-fifths of employment in 1990) paid or partially paid maternity leave is required. Personal leave of 7-30 days are required, depending on seniority.

Source: U.S. Department of Health and Human Services, Social Security Administration, *Social Security Programs Throughout the World — 1987* (Washington: GPO, 1988).

sity. The 1930s also saw a shift of public policy and authority toward the federal government and away from the states since state government tax resources were limited by the depression. In 1935, a federal Social Security program was created with a (defined-benefit) pension element and a survivors' element (the successor to the widows' pension idea). Disability insurance was added in the mid-1950s. Along with Social Security, a federally-sponsored, but state-administered, system of unemployment insurance was created. Table 2 summarizes the U.S. Social Security system (along with those of Canada and Taiwan).

Substantial growth of unionization of the American workforce began in the 1930s, in part fostered by worker discontent over the depression-related deterioration of working conditions. Changes in federal labor law and later World War II era labor policies helped solidify the growth of union representation. Public policy with regard to labor market outcomes in the 1930s thus moved toward the setting of minimums: minimum wage laws, minimum pensions through Social Security, etc. Workers who were still dissatisfied with the minimums in workplace conditions were given a mechanism — collective bargaining — to deal with their remaining problems. But they were not assured of any particular bargaining outcome beyond the minimums.

Attempts were made after World War II to create a medical insurance component of Social Security. These efforts were strongly opposed by organized medicine and failed.⁴ However, in the mid-1960s, Medicare was added to Social Security for elderly individuals (including those still working). For other, younger workers, it could be argued in the 1960s that the private system of employer-based health insurance was spreading to a larger and larger fraction of the workforce. Therefore, proponents of a universal health care system had their arguments blunted.

In essence, the current design of Social Security in the U.S. reflects the economic, political, and ideological conditions of the period from the mid-1930s to the mid-1960s. The retirement, survivors', and disability elements were implemented because the private sector (and the states) seemed unable to provide these merit goods. Effectively, the private sector provided the model but seemed unable to deliver the goods on a large scale without a strong tax incentive. With regard to health insurance, there was not private model up to the 1930s, since such insurance had not become significant. That fact, and the strong opposition of doctors, kept medical insurance out of Social Security initially. The post-World War II growth of employer-based medical insurance kept the Medicare component of Social Security limited to persons of retirement age.

basis. In many instances, the public policy issues surrounding private American benefits stem from the decentralized approach that has developed and the clash which that approach now entails in the light of a changing economy.⁶

Table 3 provides a summary of private benefit incidence in the U.S. (and the other two countries). About 45 per cent of the American workforce was covered by a pension plan in 1988. (Of these, 53 per cent had defined-benefit plans as their primary program.) Not all of these workers have vested in the plan, however. Pensions are more common among larger establishments and for full-time workers than for smaller establishments and part-timers. About 37 per cent of individuals in the workforce at some time during 1985 had employer-provided health insurance. But the figure was 63 per cent for those who worked full-time with no interruptions.⁸ Again, the incidence of health insurance coverage is lower for part-timers and workers in small establishments.

The contemporary provision of private employee benefits must be seen against a background of several influences. First, in contrast to the model of employment from the 1940s through the 1960s, there has been a weakening of employer-employee attachments in the U.S. due in part to a perceived increase in product-market uncertainty by employers. Thanks to forces such as deregulation, volatile exchange rates, and foreign competition, employers are less willing to make long-term commitments to employees. Moreover, even when such commitments are present, the wave of corporate restructuring in the 1980s demonstrated that seeming assurances are transitory. New owners may not feel obligated by practices of their predecessors. These shifts mean that, other things being equal, American employers would now prefer to offer a less generous and less secure benefit package and will resist legislation requiring them to move in the other direction.

Second, with increased worker mobility — both voluntary and involuntary — firm-level entitlements to benefits may be adversely affected by job changing. Since the American private benefit system is decentralized, where the basic unit is typically the firm, a change of employers means a shift to a new benefit system for a worker. Some benefits may have elements of portability; others may not. Yet increased product-market uncertainty and reduced employer commitments to workers implies an increased likelihood of job changing for the typical employee, perhaps involuntarily.

Third, although the overall unionization rate declined after the mid-1950s, the drop markedly accelerated in the 1980s. Unions lost considerable membership in absolute terms. By 1991, the overall union representation rate was down to 18 per cent, and 16 per cent for actual

ii. The post-World War II expansion of private benefits in the U.S.

Several factors combined after World War II to produce a substantial expansion of private employer-paid benefits in the U.S. First, during the war, wage controls discouraged wage increases but were more permissive with regard to benefits. Second, a swing to a more conservative Congress suggested that a substantial expansion of Social Security was unlikely. Issues such as health insurance would have to be handled at the employer level. Unions, particularly those attached to the CIO, began to become more interested in private benefits as a result.

Third, a Supreme Court decision in the late 1940s made it clear that benefits were within the mandatory scope of bargaining of unions.⁵ As unions negotiated new benefit plans, these spread to other union situations and to non-union employers (who were often anxious to fend off unionization by providing comparable employment conditions). Fourth, income tax coverage had expanded substantially with the growth of the federal government. Ordinary workers now paid income taxes. The tax-favored treatment of pensions and insurance, which was clarified during World War II, now became an important subsidy to employer provision of such benefits. Fifth, as benefit coverage expanded, a benefits interest group was created consisting of insurance companies, benefit consultants, and employers and unions with benefit plans. These groups lobbied Congress to widen favored tax treatment for benefits.

Note that the American pattern for private benefits became one of official fostering of employer provision through the tax code. This approach was a compromise between government provision and *laissez-faire*, a model which fit the American ideological balance. To qualify for favored tax treatment, benefits were increasingly required to meet various standards. But there were no legal requirements that employers offer benefits. Typically, benefit incidence was greater for larger firms and unionized firms than for other employers. But the late 1940s and the 1950s — the period during which the current system of fostering private employee benefits crystallized — was one in which large firms were in the ascendancy and union compensation packages were seen as setting patterns for the rest of the economy.

iii. Current provision of benefits in the U.S.: incidence and pressures

The history of U.S. benefit evolution has produced a system based on minimum provision by government through Social Security primarily aimed at retirees or others unable to work. Benefits beyond these minimums are provided on a decentralized, employer-by-employer

Table 3. Incidence and Background Information on Pensions and Health Insurance, Canada, the U.S., and Taiwan

	Canada	U.S.	Taiwan
Pensions other than Social Security	29% of private-sector labor force covered by pension, 86% of whom have defined-benefit plans. Most public workers have pensions.	45% of private-sector labor force covered by pension, 53% of whom have defined-benefit plans. Most public workers have pensions.	Under Labor Standards Law, which covers four-fifths of employees, pensions are required. Existing law specifies a lump-sum pension based on earnings and service. However, there is a significant question of compliance by smaller firms. Reforms package currently under consideration.
Health insurance other than Social Security	Some employers provide insurance supplementing government-provided system. Employer contributions to such plans are tax-deductible and not taxable to the employee.	About 87% of population is covered by some form of insurance. 89% of these have private policies and 81% of these are job-related (1988 data). 37% of wage earners with work experience had job-related insurance (1985 data).	No formal vesting required although severance pay acts as partial vesting substitute. Some firms provide vesting.

Source: William M. Mercer, Inc., *International Benefit Guidelines, 1992* (New York: William M. Mercer, 1992); Lorna M. Daily and John A. Turner, "Private Pension Coverage in Nine Countries", *Monthly Labour Review*, vol. 115 (May 1992), pp. 40-43; U.S. Bureau of the Census, *Statistical Abstract of the United States, 1991* (Washington: GPO, 1991), p. 100; Charles Nelson and Kathleen Short, *Health Insurance Coverage, 1986-88*, U.S. Bureau of the Census Report P-70, no. 17 (Washington: GPO, 1990), p. 11.

membership. For the private sector alone, the figures were 13 per cent and 12 per cent respectively.⁹ As unionization declined in the U.S., the legal and political process became seen as an alternative to collective bargaining for resolving workplace issues.¹⁰ The old 1930s idea that collective bargaining would be the main channel for employees to push for benefits above minimum standards became less tenable as the proportion of employees subject to bargaining became small. Thus, while deregulation was an important force in the product market, it did not characterize the American labor market. If anything, there seems to be a greater willingness in Congress and some state legislatures to contemplate government intervention in employee benefit matters, i.e., more (not less) labor-market regulation.

Fourth, large federal budget deficits made expansion of the Social Security system difficult as a form of labor-market intervention. Significant payroll tax increases were eventually agreed upon to pre-fund the retirement of the baby boom in the 21st century. But some elements of Social Security were explicitly cut back. The lack of a public capacity to provide benefits through Social Security has focused attention on the private benefit system.

Fifth, the American workforce is aging. Older members of the baby boom are reaching ages where concerns about pension adequacy and demands for health insurance are bound to intensify. Changing worker preferences regarding benefits generally push for "more" at a time when employer preferences are shifting towards "less".

In short, the contemporary American system of benefit provision reflects conditions of an earlier era. Some elements of the system, mainly related to private employer-based benefits, do not fit well with the modern economy. Economic forces suggest a need to externalize the benefit system. But the basic external public program, Social Security, cannot be expanded without tax increases which are the subject of fierce resistance.

iv. Current U.S. public policy issues: pensions

Most American workers who have pension coverage have a defined-benefit plan as their primary retirement program. For a long-service employee in a large enterprise with such a retirement plan, an initial replacement rate for final earnings of perhaps 60-70 per cent can be expected, with roughly 40-50 per cent coming from the private defined-benefit pension.¹¹ Unions traditionally favored such plans for several reasons. First, defined-benefit plans can be arranged to pay

benefits from the date they are created. Payments from active workers can be used to fund payments to those about to retire. Defined-contribution plans, in contrast, do not permit immediate benefits.

Second, defined-benefit plans shift a significant risk to the employer. A typical plan will pay a monthly benefit based on age, seniority before retirement, and final earnings. In contrast, defined-contribution plans simply accumulate an account for employees which can be translated into an annuity upon retirement based on such factors as the prevailing interest rate. Employees do not have a guarantee that their pension will replace a given percentage of their final earnings.

In addition, defined-benefit plans favor high seniority (long service) workers. The implicit wealth accumulation under the plan accrues largely in the later years of employment. Workers who leave their jobs early receive substantially lower pensions than those who have long careers. American economists generally find evidence that the political decision-making process of unions tilts toward the welfare of senior employees.¹² Negotiation of defined-benefit pensions is but one example.

Under a decentralized defined-benefit pension system, issues arise for job changers who leave one employer's pension for another's. The question of job mobility and pension portability led to a reduction in mandatory vesting from ten to five years in the mid-1980s. However, because the amount vested in early years of service is low, such a vesting shift addresses only a part of the mobility issue. Mobility questions become more severe for vested mid-career workers who change jobs before reaching their years of high accrual. Thus, an employee who worked consecutively for 15 years under each of two identical defined-benefit pensions will have a retirement income well below an employee who worked 30 years under one of them.

To handle the mobility and portability issues within a decentralized defined-benefit system, there would need to be an elaborate system of financial transfers between pension plans as employees changed jobs. While such reforms have been attempted in some European countries, the U.S. has not seriously considered them.¹³ Note that with an external defined-benefit system (such as Social Security) there is no mobility problem. Apart from lowered vesting, the main response has been suggestions for portable *personal* pensions and for promotion of defined-contribution pensions.

Over time, the U.S. private pension system has gravitated toward the defined-contribution approach, a natural response to decentralization of pension provision in the face of greater economic uncertainty.¹⁴ In essence, more risk is shifted to the employee in exchange for a more

mobility-compatible system. Without social concertation through public policy to externalize the private pension system, the move toward defined contribution functions as a partial substitute.

v. Current U.S. public policy issues: health insurance

Cost issues have dominated discussions of job-related health insurance in the U.S. along with issues of coverage. Medical care goods and service prices have chronically risen faster than the average price level, and there seems to be an inexorable increase in the quantity of such goods and service *per capita*. The U.S. spends more *per capita* and as a share of GNP than other countries, although gross measures of health outcomes — such as life expectancy — do not reflect the added expense.¹⁵ Employers have not proven to be highly effective cost regulators. Nor is there much reason to suppose that an employer, whose primary function is to produce particular goods and services for its customers, would also be expert in administering a health care system.

Nonetheless, since they have been saddled with primary responsibility for providing health insurance through the tax code, employers have sought ways of controlling its cost. Their solutions to cost containment involve cost shifting to employees, usually by raising deductibles or lowering the per cent of medical expenses that will be reimbursed. In addition, constraints on consumer choice (limited rationing) have been imposed.

Because of the decentralized nature of health insurance, some employer cost-control efforts go into shifting costs to someone else's plan. For example, an employee might have duplicate coverage because of a working spouse. Pushing the cost to the spouse's plan reduces expenses of one employer but raises them for another. For all plans together, such shifting amounts to a zero-sum game. The game is rational for all players *individually* but is not *collectively*. It is a symptom of lack of social concertation.

Finally, cost-control efforts often include restrictions or bans on coverage of new employees with existing illnesses. These controls produce an incentive for employees who have health problems (or whose family members have health problems) to stay with their current employers. The resulting "job lock" phenomenon is analogous to the anti-mobility effects of defined-benefit pensions. It also makes involuntary mobility (layoffs) more costly to employees with health problems. The only public policy response to this issue was a 1986 federal law requiring employers to continue offering health coverage to laid-off employees for a specified period but at *worker* expense. If the employee

can afford the cost, he or she has the advantage of paying at the employer's group rate.

Apart from cost issues, health insurance coverage has also become a public policy issue. About 14 per cent of the population under 65 years of age did not have medical coverage in 1988.¹⁶ (Persons 65 and over are almost all eligible for Medicare.) However, any system which moved coverage closer to 100 per cent would add to demand for medical services, aggravating the cost-containment problem. Hence, most proposals that have been made for coverage expansion have been accompanied by purported cost-control mechanisms.

The proposals most discussed are a national health insurance system (with government as insurer, not provider) or similar arrangements at the state level. Proponents of these approaches often point to the Canadian system (see below) and argue that, with a single payer, administrative duplication can be eliminated. They also argue that cost controls can be more effective (for example, resources would no longer be expended on shifting costs between plans).

A less ambitious approach is the so-called "play or pay" proposal. Under this system, employers would be required either to offer private health insurance to their workers ("play") or to contribute to a central fund to provide coverage for employees of firms without insurance ("pay"). Such plans, which can be national or state-run, often include some type of subsidy for smaller employers and may exempt the smaller firms. Since "play or pay" plans build on existing arrangements, and since they do not displace current health care insurers, such proposals potentially engender less opposition.

Less ambitious proposals, again federal and state, seek to increase incentives for employers to offer health insurance and subsidize private individual purchase of insurance by uncovered persons. These proposals do not seek universal coverage but rather incremental expansion. There have also been proposals to allow individuals to have tax-favored savings arrangements (as is permitted in some cases for retirement purposes) from which medical expenses could be paid. Offering the same tax advantage to individual purchase of health insurance as is offered for employer-paid insurance has also been proposed.¹⁷

As in the pension case, a fundamental difficulty with the employer-provided health insurance model is its very decentralization. The system was originally designed in an era when long careers with large firms were seen as the ideal employment model. Under such a system, issues of job mobility are unimportant. The gradual expansion of that system to more workers, combined with the impact of Medicare coverage of the elderly, created pressures for health cost inflation which indi-

vidual employers are not equipped to control. Such problems were not foreseen when the system was originally developed.

vi. Lack of social concertation in the U.S. and resultant benefit problems

There is no simple way of negotiating a new approach to defining the employment relationship in the American case. Unlike the "social partner" approach in some European countries, there are no readily-identifiable social partners in the U.S. It is therefore left to the political process to define the employment relationship, and — since issues arise in the political process on a piecemeal basis — it is difficult for politicians to see the larger picture. Pension portability concerns are not perceived as related to health plan "job lock".

What is optimal for one employer is not necessarily optimal for all. Yet it is rational, in a decentralized system, for each employer to act on a narrow micro basis with regard to lobbying for or against social legislation or in making firm-level policy. Perhaps, for example, non-portability of pensions helps firms retain workers, but each retained worker is one less worker that can be recruited by other employers, so the game is close to zero sum seen at the macro level. Pushing health care costs away from the firm and onto other firms and other providers is rational for each employer. But, taken collectively, the costs do not go away just because they are shifted. Given the ingrained decentralized norm in the U.S., it is likely that shifts in public policy toward pensions, health insurance, and other benefits will come slowly, if at all. There is no mechanism, in short, for effective social concertation.

III. A Brief Overview of Canadian Employee Benefits

Although the economies of the U.S. and Canada are closely linked, the two countries have not chosen identical paths to providing employee benefits. Canadian social security has elements closer to the British model than the American. Canadian private pensions, on the other hand, are currently broadly similar to American ones, although the regulatory and tax framework differs. Canadian health insurance more closely resembles the model in some European countries (and is similar to Taiwanese practice). The wide variation in response to similar economic conditions suggests that the options open to countries are not a simple product of economic determinism.

Various observers have noted a greater propensity in Canada for collective solutions to social problems and for more government interven-

tion. On the other hand, Canada's administration is decentralized, with provinces exercising more authority in areas such as employee benefits than the American states. Thus, major initiatives have often been made at the provincial level. Tensions between francophone Quebec and other anglophone provinces have increased the degree of governmental decentralization. Thus, Quebec operates its own public pension program parallel to the federal structure.

i. A history of Canadian private pension policy

In the late 19th and early 20th century, Canadian and American history with regard to pensions (and other benefits) was quite similar. Railroads, being large corporations with relatively good pay and long careers for employees, were among the first employers to provide pensions. By the late 1920s, the proportion of Canadian railroad workers covered by pensions was over 90 per cent, a higher percentage than in the U.S.

Banking was another sector in which Canada led the U.S. in pensions, in part because Canadian banks were not subject to the tight constraints on branch banking found in American law. A 1929 survey found Canadian pensions of the defined-benefits type¹⁸ in such diverse industries as food products, textiles, steel, rubber, paper, chemicals, petroleum, farm machinery, electrical equipment, insurance, railroads, public transit, leather, printing, retailing, and mining. Although specific information is not available, Canadian union members often belonged to affiliates of U.S.-headquartered unions, some of which had union-operated pension programs.¹⁹ Thus, it may be assumed that Canadian members also benefited from these programs.

Beginning in 1919, Canadian tax law began exempting *employee* contributions to job-related pensions (up to a specified limit) from personal income tax. In this regard, Canadian tax law differed from American: under American law, the first tax breaks for pensions were for *employer* contributions. Employers could deduct such contributions as business expenses from their corporate income taxes and employees did not have to pay immediate income tax on them. In Canada, employer contributions were made non-taxable to the employee in the late 1930s and early 1940s. Still, Canadian history has left a greater tendency for pensions to have a contributory component compared with the U.S.

A survey in the late 1930s found over 700 Canadian pension plans, although about a seventh of these were completely discretionary with the employer and had no benefit formula. As in the U.S., World War II

wage control regulations tended to favor establishing pension and other insurance plans. By the late 1940s, another survey found about a quarter of employees with pension coverage, excluding civil servants and railroad workers. This survey omitted very small firms and so probably exaggerates the rate of coverage. Only a negligible proportion of employers reported their plans to be part of collective bargaining contracts despite the size bias. It may be that Canadian employers, like their American counterparts, were anxious to keep fringe benefits away from their dealings with unions.²⁰

ii. Contemporary issues in Canadian private pension policy

During the 1980s, the proportion of private-sector workers in Canada with pension coverage stabilized at just under 30 per cent: in contrast, the U.S. coverage rate was about 45 per cent. However, while some decline was reported in defined-benefit coverage (versus defined contribution) in Canada, 86 per cent of covered workers had such plans as opposed to 53 per cent in the U.S.²¹ Thus, the defined-benefit model in Canada has held up better. Whether defined-benefit plans will do as well as in the future is an open question. The product-market ramifications of free trade with the U.S. (and possibly with Mexico) will affect Canadian labor markets, tending to undermine long-term employer-employee attachments.

Given the discrepancy in pension coverage rates between Canada and the U.S. (Table 3), Canada seems to have chosen quality over quantity, at least with regard to the private pension system.²² Canadians would apparently like their private pension system to function much like an external social security program. Thus, Canadian reform proposals have focused on mobility and portability. The easiest first step is to have a low vesting period. Thus, in Canada vesting is set at two years (as in Britain) instead of five (as in the U.S.). But quick vesting alone will not deal with other major portability problems connected with defined-benefit pensions.

During the inflationary 1970s, there was a growing interest in Canada in the possibility of indexing private pensions (in much the same manner that social security systems are often indexed). Indeed, proposals from the Canadian labor movement would have had the private pension system absorbed into social security.²³ Private pensions in Canada — as in the U.S. — are rarely indexed, although some pension reform proposals would require at least partial indexation. Indexing poses great difficulties for actuaries since small shifts in assumptions about inflation rates and asset yields can produce great swings in fund-

ing requirements. Like U.S. plans, however, Canadian pensions often make payments to retirees on an *ad hoc* basis in response to inflation. Yet the adjustments rarely fully compensate for price increases.

While the inflation problem for those already retired is easy to identify — benefits fixed in nominal terms will erode over time — there are more subtle problems for job changers. A worker who has vested in a plan and who leaves for another job (voluntarily or not) has his/her future benefit frozen in nominal terms. Inflation can thus erode the value of the pension before actual receipt. In contrast, for someone who stays in the plan to retirement age, the pension will have been set in nominal terms, but at the *end-of-career nominal wage level*. Thus, the pension starts out at a “realistic” amount even if it later erodes.

Some offset to inflation-related losses of early leavers is available in federally-regulated industries and in Ontario due to mandated severance pay. In Ontario, those involuntarily separated must be paid one week's normal salary for each year of tenure up to 26. These mandates are less generous than those found in Taiwan, where there is no pension vesting requirement (see below). Severance pay does not apply to employees who quit, i.e. cases of voluntary mobility.

It is possible in theory to create transfer arrangements so that workers can move from job to job and retire from the last employer with a pension based on career history. This outcome is precisely what social security programs provide, since they are based on total work history, not attachment to a single employer. But there are complex problems in practice in making a decentralized defined-benefit system work as if it were a single program.

Some European countries (notably Britain, whose influence on Canada is still significant) have attempted to address these problems, at least partially.²⁴ It seems likely that future pension reforms in Canada will focus on the mobility concern. However, it must be noted that Canadians have been talking about mobility and inflation issues since the 1970s without adopting full-fledged changes in pension regulations.²⁵ The lack of solutions to the technical issue of pension coordination illustrates the practical difficulty of externalizing an internal benefit system.

British policy in the 1980s also emphasized personal pensions as a mobility solution and this might eventually have an impact on Canada. Personal pensions (Registered Retirement Savings Plans) exist in Canada. They can be primary retirement income vehicles for those without pensions, such as the self-employed, but those under job-related pensions can also make limited contributions to them.

iii. Social security pensions in Canada

There is a seeming paradox in the fact that Canada's social security system dates from the early 1950s while the American system began in the mid-1930s. Both countries went through the Great Depression, and it might be supposed that Canada — with its apparently greater proclivity for implementing collective solutions to social problems — might have come earlier to social insurance than the U.S. But for social security that did not happen.

It appears, with hindsight, that the implementation of Canadian social security was delayed by this proclivity. English-speaking Canada loosely focused on British practice of providing local poor relief in the 19th century, while Quebec was influenced by Catholic social doctrines.²⁶ Ideas of public pensions for the indigent elderly, based on developments in other countries, ultimately produced the Old Age Pensions Act of 1927, which provided a federal subsidy of 50 per cent to provincial means-tested pensions. Although some states in the U.S. had implemented such pensions, there was no federal role (or subsidy) in America prior to 1935 (the American Social Security Act). An existing federal program of means-tested pensions in Canada reduced the pressure for a more general social security system without means testing.

Social security pensions arrived in two stages in Canada. Although the American social security model was discussed in Canada, it did not dominate the early debate and the system initially created did not resemble American social security.²⁷ A “universal pension” system was adopted in 1951, providing a retirement benefit based on length of residence in Canada, but not on past earnings, similar to the flat-rate pension found as the first tier of the modern British system. The Canadian flat-rate pension was funded by general revenue rather than payroll taxes. As in Britain, the existence of earnings-linked pensions in the private sector established a model for an eventual second tier of social security, based on earnings and funded by employee and employer taxes.

In the mid 1960s, the Canada Pension Plan — for all provinces but Quebec — and a parallel Quebec Pension Plan were established, forming the second tier of Canada's social security system. This time, despite the similarities with developments in Britain, the American social security system was explicitly cited as a model. Perhaps for that reason, an option for private pensions to contract out of the second tier of social security was not provided, which represented a deviation from the British model.

iv. Health insurance in Canada

While the Canadian pension system and (part of) the social security retirement system have similarities with American practice, its health insurance arrangements are totally different. To the extent that there have been cross-border spillovers between the two countries, they have in recent years gone from Canada to the U.S.: there have been proposals in the U.S. of adopting a Canadian-style system and some interest in Congress in considering it.²⁸ Indeed, the Canadian model has achieved so much attention in the U.S. that the American private health care industry has taken pains to criticize it.²⁹ Canada spends significantly less than the U.S. on health *per capita*, although it ranks second in health spending relative to GDP compared with other OECD countries.³⁰

The basic Canadian health insurance plan — generally known as Medicare — is provided to all residents at the provincial level with federal subsidy.³¹ Some provinces supplement general revenue with payroll taxes or resident-paid premiums (when such premiums are paid by employers, they are treated as taxable benefits). Provincial authorities negotiate with private health providers and establish fee schedules. They also provide direct funding of certain hospital capital expenditures.

The level of the fee schedule and the degree to which doctors are allowed to charge fees above the official prices have been subjects of tension between doctors and provincial governments. Strikes over this issue have occurred. Indeed, the position of doctors towards a government health insurance program has revolved around the fee-setting issue since the mid-1940s when the issue was first seriously considered. At that time, Canadian doctors took a cautious view of the issue, suggesting that they would not oppose a government insurance system as long as fee setting remained a private matter, a position was similar to that of American doctors during the World War I era. But, as American doctors had done earlier, they later opposed government health insurance of any type, fearing inevitable controls on fees.³²

Despite doctors' opposition, government programs gradually extended in Canada from a means-tested approach to the current Canada Health Care Act of 1984 which consolidated previous programs and removed direct fees to patients beyond the schedule of reimbursements received under provincial programs. In effect, price rationing was removed under provincial programs. In effect, price services to other means.³³ However, patients can — at their own expense — purchase certain services beyond the basics (such as private

hospital rooms). Employers often provide supplementary health insurance policies to handle such expenses. Employer contributions to such plans are tax deductible and not taxable to the employee: above a specified level they receive favorable tax treatment.

The American debate over the Canadian model has revolved around the degree to which Canadian-style rationing would be accepted in the U.S. Issues have been raised about access to new technology, and it has been argued that Canadian patients have the safety valve of access to the U.S. medical market place. In some cases, Canadian authorities have paid for patients to use American providers. However, *de facto* non-price rationing has also been creeping into the American system as part of cost-control efforts. And some have argued (in reverse) that Canadian doctors now have more "professional autonomy" than their U.S. counterparts.³⁴

These debates, however, do not address the labor-market consequences of the Canadian approach to health insurance. Although supplementary medical insurance is a common employee benefit in Canada, the fact that basic expenses are paid by the provincial plans means that medical care has been externalized from the firm viewpoint. Thus, the mobility barriers found in the U.S. due to company-by-company health insurance are not experienced in Canada. A Canadian worker who loses a job, or who changes jobs, need not fear a loss of a basic health insurance entitlement.

v. The Canadian approach: a summary

Overall, Canada has shown a greater propensity than the U.S. for government intervention in the labor market. In gross terms, the two countries are similar with regard to pensions: social security pensions are external to the employer; private pensions are internal. Canada seems to have a greater reliance on the defined-benefit pension model than the U.S. — the kind of plan under which mobility is most difficult. On the other hand, Canada seems to be more aware of the mobility problem and its link to inflation. It has a lower vesting period than the U.S. and is considering other devices to make pensions more portable. In the health care area, Canada has almost totally externalized medical insurance from the employer by providing a universal entitlement. Labor mobility was not the major force behind the creation of this system. Nonetheless, an external medical insurance system provides a better fit to a labor market buffeted by outside pressures than the U.S. internal-to-the-employer system.

IV. A Brief Overview of Taiwanese Employee Benefits³⁵

Although public policy in labor matters in the Republic of China goes back to the pre-1949 period on the mainland, current policy is mainly a reflection of post-1949 policies and the rapid growth Taiwan has experienced over the past two decades. As in the U.S. and Canada, there is a mix of public and private benefits. However, the Taiwanese format of public benefit delivery is different, especially with regard to pensions. And, for those benefits which fall in the private area, the role of the state as a mandator of what will be provided by employers is substantially greater.

A key aspect of the private benefit system in Taiwan, especially with regard to retirement income, is its state of flux. Because of the large role of the state, the eventual outcome will be determined by law, although with significant interaction with private employers. Private employers — many of which are small — have been vocal in opposing mandates they consider burdensome to business. A major issue to be faced is the degree to which the eventual benefit system will be internal or external to the firm.

i. Social security in Taiwan

The social security system — usually translated into English as “labor insurance” despite its government administration — dates back to a law of 1950 which, in turn, was enacted pursuant to a provision in the 1946 (mainland) constitution. Thus, it is a much more recent creation than the social security system of the U.S. Except for the self-employed, where there is a government contribution, the Taiwanese social security system is funded by mainly employer and employee payroll taxes.³⁶ Coverage of the social security system was extended after its initial creation. Employees of the smallest firms — with four or fewer workers — are not covered. However, at the end of 1990, 6.9 million persons were covered, over four fifths of total employment. In contrast, in 1980 only 2.5 million persons were covered (less than 40 per cent of employment).³⁷

Table 2 summarizes the key elements of the current version of Taiwanese social security. As can be seen, under social security, employees are entitled to retirement, disability, and medical benefits as well as compensation for industrial injury. These benefit entitlements are therefore portable from employer to employer. The retirement benefit is defined in the sense that it reflects past earnings. However, it is

paid in a lump sum, a different approach to that found in the U.S. or Canada.

The retiree (or disabled worker) receives a fixed payment related to service and to past earnings. It is then left to the recipient to make arrangements to spread this income over his/her remaining lifetime. In principle, the recipient could purchase an annuity from a commercial insurance carrier for this purpose. However, most recipients do not use this option. Thus, Taiwanese social security benefits differ from the type of defined benefits found in the U.S. and Canada which continue on a monthly basis indefinitely (and with inflation-linked adjustments).

A retiree faces an element of risk linked to earnings on financial assets available *after* retirement, even if an annuity is purchased, similar to that faced under a defined-contribution system. On the other hand, retirees need not be concerned with returns on financial assets *prior* to retirement, since the lump sum is linked only to seniority and past earnings. In that respect, the system is similar to a defined-benefit plan. Thus, the Taiwanese social security system is a cross between the two types of plans.

While the lump-sum feature may seem unusual to observers used to North American and European social security programs, it should be noted that one of the other “four tiger” countries — Singapore — utilizes a similar approach. Use of a lump sum seems to be linked to the Chinese tradition of bonus payments on certain holidays and for other purposes: the lump sum can be viewed as a formalization and adaptation of the bonus practice. Additionally, there is also a tradition of family care of the elderly, and the lump sum can be viewed as a contribution to the family of the recipient to assist in such care. Finally, there is an element of trust. Chinese retirees prefer to receive their retirement wealth in a single payment rather than rely on a promised future stream of payments from an institution. A promise may not be kept while a lump-sum payment leaves each retiree’s fate in his/her own hands.

Of course, living patterns are changing in Taiwan as it rapidly industrializes and dependence on family members for old age support may become less of a norm. In the future there may be receptivity to a move from the lump-sum approach to the kind of monthly payment found in the U.S. and Canada. Such countries as South Korea and Japan use the monthly pension approach for social security, so oriental role models are available. Indeed, there is currently a proposal to modify social security in Taiwan and provide monthly payments. This proposal is linked to a mandated modification of the current private pension system.

use benefits as a way of retarding outward labor mobility in their own interests.

Two pieces of legislation strongly influence the private benefit system in Taiwan. The 1984 Labor Standards Law mandates a variety of benefits relating to retirement, other departures and work-related disability, but it covers employers only in seven designated industries.⁴³ An estimated 40 per cent of the workforce is not covered: major omissions are in the retail and service areas.

The government's intent is to extend the Labor Standards Law to cover all employers. However, it is unclear that compliance is being fully achieved across all employers now covered, partly because the details of the law's mandates are still being developed and ambiguities remain. In any case, employers not covered by the Labor Standards Law are instead covered by an older (originally mainland) Factory Act which dates from 1931. Although the Factory Act also has certain benefit mandates, they are less extensive than those of the Labor Standards Law. And again, issues of compliance exist, especially among smaller firms.

iii. Private pensions in Taiwan

A summary of legal requirements regarding benefits appears in Table 3. Under the 1984 Labor Standards Law, covered employers must provide a private pension. Before that time, only government-owned enterprises were required to have pension systems under legislation going back to the mainland period. The retirement benefit under the Labor Standards Law private pensions is similar in format to the existing social security pension. That is, it is delivered as a lump sum linked to final earnings and seniority upon retirement.

As the law now stands, employers must prefund these pensions, using designated government financial institutions; they thus have less freedom than American employers to determine financial asset policy. Pension plans are required to be administered by a board consisting of company and worker representatives. Technically, there are no vesting requirements, but — because there is also a requirement under the Law that employers provide a severance benefit related to earnings and past seniority — a *de facto* partial vesting exists for involuntary terminations. (More on this point below.) In addition, employers may provide some form of vesting voluntarily. Employers not covered by the Labor Standards Law need not provide pensions, although they may do so voluntarily.

ii. Private benefits in Taiwan: general background

As noted, the private benefit system is in a state of flux, largely because of public policy initiatives. Average firm size in Taiwan is smaller than in the U.S. or Canada. But, by law, firms of any significant size generally have a welfare fund covering activities reminiscent of (voluntary) turn-of-the-century welfare work in the U.S.³⁸ For example, the fund might be used for emergency loans, recreational activities, housing finance, etc.

Early American and Canadian welfare work had a decidedly paternalistic element. In Taiwan, such elements are also present, in part stimulated — or at least reinforced — by government efforts such as a 1982 campaign to “turn the factory into family, turn the factory into school”.³⁹ Paternalism during the early 20th century in the U.S. and Canada also had a union-avoidance aspect. The modern linkage in Taiwan between benefits and industrial relations concerns also is in part due to labor-relations concerns, but the history is quite different.

During the period of martial law — from the move of the Republic of China government from the mainland to Taiwan until 1987 — company unions in Taiwan existed in firms of significant size under government and management tutelage. With the lifting of martial law and the general political liberalization, came concerns that labor relations might enter a phase similar to the turmoil evident in South Korea. Unionization of the labor force, which was growing even before the lifting of martial law, jumped from 23 per cent in 1987 to 33 per cent in 1990.⁴⁰ In fact, Korean-style turmoil has not occurred in Taiwan, although elements of independent industrial relations have emerged.⁴¹ Nonetheless, employee benefits have been seen by government as part of a larger program to encourage labor-management cooperation and harmony and to avoid confrontation.

The economic background must also be considered. Like the other “four tiger” countries and Japan, unemployment rates have been quite low in Taiwan. Indeed, the situation could generally be characterized as a labor shortage. During the late 1980s and early 1990s, roughly 15–20 per cent of the Taiwanese labor force changed jobs, entered the labor force, or left the labor force on an annual basis.⁴² These types of employment flows have implications for private benefits. For example, such shifts in work status represent breaks in service which would typically terminate pension credits with an individual employer. A benefit system which is incompatible with job-status changing creates obvious tensions with social objectives in a society in which such changes are common. By the same token, employers might well want to

An alternative approach would be to operate the pension system as a second tier of social security. The employer's liability for a pension would be satisfied by paying into a central fund which would then pay a retirement benefit based on a worker's lifetime employment history (with all employers). It is unclear whether such an arrangement will evolve. Under one proposal, long-service workers would receive a monthly pension from the Labor Standards Law plan plus the existing lump sum from the first tier of social security. Shorter-service workers would receive a lump sum from both programs (assuming the social security component does not switch to a monthly pension). Workers with existing pensions would be allowed to choose whether to continue under their old arrangements or switch to the new system.

Those without pensions and all new hires would be under the new system. If the retirement system evolved toward a second multi-employer pension, the system would thus be external to the firm, except for those who now have pensions and choose to keep them: such numbers would steadily dwindle as a proportion of the workforce.

iv. Taiwanese severance pay and employer incentives

As noted, because severance pay is currently significant in magnitude and accumulates with seniority, it can be viewed as a kind of pension adjunct in cases of involuntary termination. Taiwan is a country with a chronic labor shortage and the existing severance pay system may play some role in this phenomenon. Severance pay gives employers an incentive to arrange their personnel practices so that people quit (and thereby lose their severance pay entitlement). Quits are cheap; terminations are expensive for employers under the present system.

There was general interest among economists in the mid-1980s in the use of alternative pay systems to stimulate employment and reduce business-cycle unemployment. In particular, Martin Weitzman proposed the use of profit sharing to create such incentives.⁴⁵ As he originally posed the issue, profit sharing reduced the marginal cost of hiring, shifting the economy toward a chronic labor shortage. Business downturns then consisted largely of "laying off" vacancies rather than actual employees, thus producing job stability.

While there is some private use of profit sharing in Taiwan, the severance pay practice is more ubiquitous, since it is required under both the Labor Standards Law and the Factory Act (although the requirement is less generous under the latter). The severance pay requirement should stimulate employers to want quits, other things equal: one way to stimulate quits is to set pay lower than it would be otherwise, relative to the

Payments to fund pensions up to 15 per cent of payroll pursuant to the Labor Standards Law are deductible to the employer under corporate tax law and are not taxable to the employee at the time of contribution. For employees designated as "laborers" no tax occurs at the time of pension receipt; for others 50 per cent of the pension is subject to income taxation. (All employees covered by the Labor Standards Law are so designated.) Employees not under the Labor Standards Law who have voluntary pensions are allowed similar tax treatment but the ceilings are lowered. Such employers with prefunded pensions have an eight per cent, instead of 15 per cent, ceiling. Those with "book reserve" pensions (unfunded plans) have a four per cent ceiling.

As noted, a key aspect of the Labor Standards Law is non-compliance and employer resistance, especially among smaller employers. A major issue behind the resistance has been retroactivity of pension benefit entitlement to the period before 1984. However, it appears that the government will not include retroactivity in its pension reform proposals. Much remains to be clarified about how the law will be implemented.

Apart from the retroactivity question, there are two other key areas of uncertainty. First, there is interest in converting the pension system to one in which a monthly payment, rather than a lump sum, will be paid. Employers appear to be in favor of some kind of monthly option, perhaps in conjunction with a lump sum.⁴⁴ Second, it is unclear whether pensions will be made internal or external to the firm.

Under the present Labor Standards Law, there is no pension vesting and pensions are internal. With small firms (who may readily go out of business) and a tight labor market (with attendant labor turnover), many employees may never qualify for a pension. And even for those that do, much of their work experience may not have been with employers where they achieve pension eligibility. Thus, with the law in its current form, pensions would nominally cover a large fraction of the workforce. An estimated 60 per cent of the workforce is covered by the Labor Standards Law, but the coverage would be illusory for many.

For certain workers, however — those close to age-service qualifications for a pension — there are strong anti-mobility incentives under the current system. And there are also artificial incentives to discharge such workers, assuming the employer's contributions are experience-rated. Although employers who discharge workers become liable for severance pay, the severance pay due will be significantly less than the pension. Such issues have reportedly already arisen under current arrangements and are the subject of the equivalent of wrongful-discharge litigation.

market average. Since all firms cannot pay below average, however, the eventual outcome (in theory) would be a lower than market-clearing wage and a chronic labor shortage.⁴⁶ Although disadvantages could be cited for artificially stimulating a labor shortage, such a shortage has many social benefits associated with full employment and more job security.

While there may be socially desirable attributes of the severance pay system as it presently operates, recent proposals have called for capping the severance requirement to four months' pay. This proposal would end the open-ended liability which increases with yearly service. The rationale for the cap is that severance pay could be viewed as an unemployment benefit and four months should be adequate time to find a new job. In addition, if the pension system switches to an external-to-the-firm second tier of social security, there would be no need to have severance pay as a *de facto* form of partial vesting. To the extent that severance pay has functioned as source of full employment, however, a cap would reduce its impact on the macro economy.

v. Health insurance in Taiwan

For most workers, health insurance under social security is their only source of coverage. Private providers supply the actual service under a fee schedule negotiated with the government. Some co-payments may be required under the system for patients but most of the costs of medical care are provided by the central fund. With health insurance thus external to the firm, the anti-mobility incentives found in the U.S. due to pre-existing illness limitations (or merely loss of coverage) are removed.

Higher-paid employees in Taiwan may also have private employer-provided supplements, giving them a choice of going outside the basic social security network. There may be pre-existing illness limitations in such plans as in the U.S. But because they cover relatively few employees, and because those under private health insurance can always fall back on the social security system, the anti-mobility incentive is decidedly less important than in the American case.

vi. The future of employee benefits in Taiwan

Despite its emphasis on relatively free markets, Taiwan has subjected its employee benefit system to government regulation. Basic pensions and health insurance are provided by social security. Private pensions

and related severance pay practices are regulated by law. Both may be drastically changed by recent official proposals.

To the extent that the ultimate decision is to externalize the pension system, Taiwan will have a benefits package that accords well with a labor force in which employee mobility is a characteristic. On the other hand, if pensions are established which are not portable and have no vesting, barriers to mobility will be created. Taiwan has the advantage of making its decisions about employee benefits in the contemporary setting. It is thus less likely to be saddled with practices out of keeping with a modern economy than countries which established their patterns of employee benefits a long time ago. To that extent, Taiwan can be viewed as a model for EC countries now reviewing their benefit policies in the context of economic integration.

V. Lessons from the Three Countries for European Integration

Recent economic theorizing about employee benefits — especially pensions — has emphasized optimality and efficiency in employer decision-making. It should be apparent, however, from this survey of the U.S., Canada, and Taiwan that how employers act in the benefits area is heavily affected by public policy. Some kinds of benefits employers offer — retirement income and health insurance in particular — are regarded by governments as merit goods. Government thus takes a major role in regulating and requiring their provision. An important general policy option is the degree to which such merit goods are to be provided through systems internal or external to the individual employer.

Generally, EC countries can expect their product markets to become more competitive and uncertain as integration and harmonization proceeds. Benefit programs which are external to the enterprise are better suited to handle the resulting pressure for labor mobility. The external approach still leaves a wide range of options ranging from direct government provision (the long-standing German social security model) to quasi-private/quasi-public institutions (French occupational pension funds) to individualistic solutions (tax-favored personal pensions of the type now being fostered in Britain). In addition, internal arrangements can be pushed in the direction of portability (Dutch and British efforts to allow workers to carry over entitlements from one company pension to another). That is, with appropriate regulation, internal arrangements can be externalized.

The key point is that arrangements such as retirement income and access to health care will not simply evolve in an optimum direction based on pressures from the product market. Adam Smith's "invisible hand" is too weak to alter structures with long histories and vested constituencies, particularly since there has already been heavy government involvement in creating the existing institutions. EC countries can take advantage of the general set of concerns which have been placed within the Social Europe category to modernize their employee benefit systems.

Notes

¹ In describing the systems in the U.S., Canada, and Taiwan, three source books have been helpful. These are U.S. Department of Health and Human Services, Social Security Administration (1988) *Social Security Programs Throughout the World - 1987*, research report no. 61, GPO, Washington; William M. Mercer, Inc., (1992) *International Benefit Guidelines 1992*, Mercer, New York; Swiss Life (1990) *Employee Benefit Reference Manual 1990*, Swiss Life, Zurich.

² See Mitchell D. J. B. (1991) "Social Insurance and Benefits", Working Paper 201, UCLA Institute of Industrial Relations, for more details.

³ Mitchell D. J. B. (1992) "Employers' Welfare Work: A 1913 BLS Report", *Monthly Labor Review*, Vol. 115 (February), pp. 52-55.

⁴ Poen M. M. (1979) *Harry S. Truman Versus the Medical Lobby: The Genesis of Medicare*, University of Missouri Press, Columbia, MO.

⁵ Inland Steel Co. versus NLRB (1948).

⁶ Mitchell D. J. B. (1990) "Employee Benefits and the New Economy: A Proposal for Reform", *California Management Review*, Vol. 33 (Fall), pp. 113-130.

⁷ Dalley L. M. and Turner J. A. (1992) "Private Pension Coverage in Nine Countries", *Monthly Labor Review*, Vol. 115 (May), pp. 40-43.

⁸ Nelson C. and Short K. (1990) *Health Insurance Coverage, 1985-88*, Current Population Report P-70, no. 17, GPO, Washington, p. 11.

⁹ Source: U.S. Bureau of Labor Statistics (1992) *Employment and Earnings*, Vol. 39 (January), pp. 228-229.

¹⁰ Examples include an upsurge in court litigation over wrongful discharge by individuals and federal legislation in 1988 requiring 60 days advance notice before mass layoffs and plant closings.

¹¹ The percentage coming from the private pension will erode over time since Social Security is indexed to price inflation while the private pension will not be. Data refer to a person earning \$20,000-\$35,000 with 30 years at the firm. Source: U.S. Bureau of Labor Statistics (1990) *Employee Benefits in Medium-to-Large Firms, 1989*, GPO, p. 96.

¹² Freeman, R. B. and Medoff J. L. (1984) *What Do Unions Do?*, Basic Books, New York, chap. 8.

¹³ Mitchell D. J. B. and Rojo Jacques (1991) "Employee Benefits in the Context of Europe 1992", Working Paper no. 191, UCLA Institute of Industrial Relations.

¹⁴ Gustman A. L. and Steinmeier T. L. (1992) "The Stampede Toward Defined Contribution Pension Plans: Fact or Fiction?" *Industrial Relations*, vol. 31 (Spring), pp. 361-369.

¹⁵ Source: U.S. Bureau of the Census (1991) *Statistical Abstract of the United States, 1991*, GPO, Washington, pp. 834-835, 839.

¹⁶ U.S. Bureau of the Census, *Statistical Abstract of the United States, 1991*, op cit., p. 100.

¹⁷ For a proposal to allow individuals to have tax deductions for health care, see Haislmaier, Edmund F. (1988) *Minimum Health Benefits Act: Mandating New Problems*, issue bulletin 136, Heritage Foundation, Washington.

¹⁸ Latimer M. W. (1932) *Industrial Pension Systems in the United States and Canada*, Industrial Relations Counselors, New York, vols. 1 and 2, pp. 20-35, 36-39, and appendices.

¹⁹ Latimer M. W. (1932) *Trade Union Pension Systems and Other Superannuation and Permanent and Total Disability Benefits in the United States and Canada*, Industrial Relations Counselors, New York.

²⁰ Canada, Dominion Bureau of Statistics (1950) *Survey of Pension and Welfare Plans in Industry, 1947*, DBS, Ottawa, pp. 1, 6, 9 and 23.

²¹ Conklin D. W. (1991) "Pension Policy Reforms in Canada" and Wolfson M. C. (1991) "An Overview of Statistics Relating to Private Pension Plans in Canada" in Turner J. A. and Dalley L. M. (eds.), *Pension Policy: An International Perspective*, GPO, Washington, pp. 73-101 and 103-115.

²² It should be noted, however, that there is uncertainty with regard to Canadian pension coverage data. June Dewetering, for example, gives an estimate of pension coverage for Canada roughly in line with the American data. See her "Occupational Pension Plans: Selected Policy Issues", background paper BP-250E, Canada, Library of Parliament, February 1991.

²³ Pesando J. E. (1979) *Private Pensions in an Inflationary Climate: Limitations and Policy Alternatives*, Economic Council of Canada, Ottawa.

²⁴ Mitchell and Rojo, "Employee Benefits in the Context of Europe 1992", op. cit.

²⁵ Economic Council of Canada (1979) *One in Three: Pensions for Canadians to 2030*, ECA, Ottawa, chap. 7; Pesando J. E. and Rea Jr., S. A. (1977) *Public and Private Pensions in Canada: An Economic Analysis*, University of Toronto Press, Toronto, chaps. 2-4.

²⁶ Material which follows was drawn from Kenneth Bryden (1974) *Old Age Pensions and Policy-Making in Canada*, McGill-Queen's University Press, Montreal.

²⁷ Official documents refer to the U.S. social security system along with systems of other countries. See Canada, Joint Committee on Old Age Security (1950) *Report of the Joint Committee of the Senate and House of Commons on Old Age Security*, Controller of Stationery, Ottawa.

²⁸ U.S. General Accounting Office (1991) *Canadian Health Insurance: Lessons for the United States*, GAO/HRD-91-90, GAO, Washington.

²⁹ Neuschler E. (1990) *Canadian Health Care: The Implications of Public Health Insurance*, Health Insurance Association of America, Washington.

³⁰ Schieber G. J. and Poullier J.-F. (1989) "International Health Care Trends: 1987", *Health Affairs*, vol. 8 (Fall), pp. 169-177.

³¹ Note that both Canada and the U.S. have programs described as "Medicare". The Canadian program, however, is comprehensive while the U.S. program covers only the elderly. Hence, the use of the same name for the programs can be confusing.

³² Stevenson H. M., Williams A. P. and Vayda Eugene (1988) "Medical Politics and Canadian Medicare: Professional Response to the Canada Health Act", *Milbank Quarterly*, vol. 66 (1), pp. 65-104.

³³ Deber, R. B. (1991) "Philosophical Underpinnings of Canada's Health Care System", *Canada-U.S. Outlook*, vol. 2 (September), pp. 20-45.

³⁴ Evans R. G. et al. (1989) "Controlling Health Expenditures -- The Canadian Reality", *New England Journal of Medicine*, vol. 320 (March 2), pp. 571-577.

³⁵ Apart from other sources, material that follows reflects information from Wyatt Company, Taiwan Branch (1992) *Compensation Report, Taiwan*, Wyatt, Taipei.

³⁶ Certain government contributions are made for special groups in the workforce.

³⁷ Source for coverage data: Taiwan, Bureau of Labor Insurance for Taiwan-Fukien Area (1991) *Statistical Data for Taiwan-Fukien Labor Insurance*, Bureau of Labor Insurance, Taipei, p. 402. Source for employment data: U.S. Department of Labor, Bureau of International Labor Affairs (1991) *Foreign Labor Trends, Taiwan*, report no. FLT 91-51, GPO, Washington, and earlier editions.

³⁸ The legal requirement to have a welfare fund is traceable to a 1943 (mainland) law.

³⁹ Chao S.-P. (1989) *Labor Policy and Labor-Management Relations in the Republic of China on Taiwan*, Council of Labor Affairs, Taipei, p. 22.

⁴⁰ Data from U.S. Department of Labor, Bureau of International Labor Affairs (1991) *Foreign Labor Trends, Taiwan 1990-1991*, report FLT 91-51, GPO, Washington, and earlier editions.

⁴¹ Kleingartner A. and Peng H.-Y. (Shara) (1991) "Taiwan: An Exploration of Labour Relations in Transition", *British Journal of Industrial Relations*, vol. 29 (September), pp. 427-445.

⁴² Taiwan, Directorate-General of Budget, Accounting and Statistics (1992) *Report on the Manpower Utilization Survey, Taiwan Area, Republic of China, 1991*, Council for Economic Planning and Development, Taipei, p. 54.

⁴³ The seven covered industries are (1) agriculture, forestry and fishing, (2) mining and quarrying, (3) manufacturing, (4) construction, (5) water, electricity, and gas, (6) transportation, warehousing, and telecommunications, and (7) mass communications.

⁴⁴ A survey of employers suggested that many would prefer a system with monthly payments, at least as an option, to a lump-sum-only system. Source: Taiwan, Bureau of Labor Insurance for Taiwan-Fukien Area, *Statistical Data for Taiwan-Fukien Area Labor Insurance*, op cit., Table 120.

⁴⁵ Weitzman M. L. (1984) *The Share Economy: Conquering Stagflation*, Harvard University Press, Cambridge, MA.

⁴⁶ In effect, this is a reverse of the efficiency-wage argument. Under efficiency wages, employers receive a benefit in terms of higher productivity or lower turnover costs by trying to pay more than average. Since they all cannot pay above average, the result is a "too-high" wage and unemployment. In this severance pay case, however, employers receive a benefit (not having to pay for severance) if the employee quits. They thus have an incentive to pay below average. Since all cannot pay below average, the result is a "too-low" wage and a labor shortage.