

# **The Politics of Reforms in Bismarckian Welfare Systems: The Cases of Czech Republic, Hungary, Poland and Slovakia**

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Paper presented at the conference

"A long good bye to Bismarck?  
The politics of welfare reforms in Continental Europe"

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June 16 - 17, 2006

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## **Abstract**

This paper briefly explores the social policy developments in Czech Republic, Hungary, Poland and Slovakia since the first establishment of Bismarck institutions in the period antecedent to the end of World War II. In particular, it asks how and to what extent Bismarck institutions survived, adapted and evolved during the communist and post-communist social policy re-organization, as well as asking what is the new internal structure of these welfare states in transition. The main argument is that the four Vizégrad countries have built their contemporary welfare state on the ruins and with the ruins of the welfare state they had previously introduced, and that these welfare states are facing a process of internal restructuring that leads to a hybridization of the system. The paper also identifies four main welfare reform trajectories occurring since World War II. These correspond to: the *golden age*, the *era of forced expansion*, the *era of retrenchment's attempts* and the *era beyond retrenchment*.

## **Introduction<sup>1</sup>**

In 1989 Central and Eastern European policy makers were suddenly confronted with the difficult task of restructuring a welfare state under a complete different economic and political system. The restructuring of welfare institutions accompanied the emergence of new and serious societal problems. More and more people were hit by unemployment and poverty, the family pattern in force during communism had to be re-discussed, and also protection during old age and sickness had to be renegotiated. Reforms started immediately and involved important structural changes. The four Vizégrad<sup>2</sup> countries (Czech Republic, Hungary, Poland and Slovakia) raised retirement age and pension insurance contributions while reducing the pay-as-you-go principle, introduced health insurance while guaranteeing the access to health care through the obligation of the state to ensure unprotected citizens, implemented a German-like unemployment insurance consisting usually of three pillars (unemployment benefits, unemployment assistance and social assistance), reduced the excessive family benefits heritage of the communist system while continuing to pursue a pro-natalist policy making and long-term child care (very often until the child is enrolled in university education), as well as establishing a basic safety net for those citizens at persistent risk of poverty.

Such transformation was certainly not without pain, since it implied a redefinition downwards of rights and responsibilities, previously generously granted by the state-paternalist welfare state. According to what principles will the new society be based? What kind of democracy will be introduced? And, more importantly, what kind of social security system should be established in order to ensure a smooth transition from central planned economy to a market economy? For policy-makers of the region, these were not highly abstract questions, but practical and urgent ones.

Despite the fact that great attention has recently been given to the role played by institutions and path-dependent mechanisms in the development of European welfare states (see, for instance, Immergut 1992, 1998, 2005; Bonoli and Palier 1998, 2001; Pierson 1996, 2000, 2004; Thelen 2004; Streeck and Thelen 2005; Ebbinghaus 2005, 2006), the possible outcome of such institutional transformations are still object of a

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<sup>1</sup> In writing this paper I have, directly and indirectly, benefited from several discussions, comments and critiques. I must give particular mention to François Bafail, Daniel Clegg, Michael Dauderstädt, Frank Ettrich, Heiner Ganßmann, Karl Hinrichs, Nick Manning, Philip Manow, Julia O'Connor, Bruno Palier and Vivien Schmidt. It goes without saying that whatever faults remain are entirely my own responsibility.

<sup>2</sup> In February 1991, Czechoslovakia, Hungary and Poland met in the city of Vizégrad (Hungary) and agreed on a "Declaration of Cooperation on the Road to European Integration", which represented the first attempt to establish a common platform to discuss their future in Europe.

controversial debate. Here, the main problem is to characterize, in a clear manner, the new internal configuration, which results from a continuous process of structuring, de-structuring and restructuring of existent welfare institutions<sup>3</sup>. The literature usually addresses Central and Eastern European welfare states as extremely diverse and doomed to follow, on a country basis, one of the Esping-Andersen's (1990) three-fold typology. For Bob Deacon (1992), Poland should have become a good example of "*post-communist conservative corporatist*" welfare state, the Czechoslovakia of a *social democratic* model, while Hungary a liberal welfare regime. More recently, Zsuzsa Ferge (2001) and Erzsébet Szalai (2005a) have expressed their worries that Hungary might be on the move towards the liberal welfare regime, whereas another Hungarian political scientist, Julia Szalai (2005b), has affirmed that in Hungary, a mixture of corporatism and liberalism, was, in reality, the main characteristic of the new welfare state. None of these authors, however, has paid serious attention to the commonalities that the four Vízegrad countries shared, even though it would have been interesting to understand how Bismarck institutions in force before World War II were adapted to the universal communist principles and, then, eventually recombined in the new post-communist environment.

This paper aims at addressing this issue by asking how and to what extent Bismarck institutions survived the communist and post-communist social policy re-organization, as well as what is the new internal structure of these welfare states in transition. As anticipated in previous work (Cerami 2005), Central and Eastern European countries seem to develop around a new welfare logic, which combines, in a path-dependent and innovative way, components of Bismarck social insurance, of communist egalitarianism and of liberal market orientation. In short, it includes elements of each of the Esping-Andersen's three-fold classification.

Contrary to common assumptions that look at the establishment of welfare institutions as being implemented by design or as the result of an aseptic *policy transfer*, this paper will argue that the four Vízegrad countries have built their contemporary welfare state on the ruins, and with the ruins, of the welfare state they had previously introduced in the pre-communist and communist period. The reason for the inclusion of these countries in the family of Bismarckian welfare states lies, therefore, not only in the fact that they have a long tradition of Bismarck social insurance and are usually considered the front-runners of reforms that might be implemented elsewhere<sup>4</sup>, but also in the fact that Bismarck

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<sup>3</sup> For the concept of "structuring, de-structuring and restructuring" welfare institutions, see Bartolini (2005) and Ferrera (2005).

<sup>4</sup> The three-pillar scheme of pension was introduced in Hungary and Poland well before it was tested in Western Europe. Similar considerations can be made for the NDC (notional defined contribution), which was launched in Latvia in January 1996 and in Poland well before it was introduced in Sweden and Italy.

institutions, established before World War II, lived, adapted and evolved during the communist social policy re-organization from 1945 to 1989, and also succeeded in surviving the, perhaps, even more rapid structural transformation following the dissolution of the central planned economy.

For the purpose of fluidity, after briefly summarizing the economic and political situation of the four Vizégrad countries, as well as discussing the influence that *policy discourses* and international organizations had on national policy outcomes, the transformation, and the origins of these welfare states in transition in the main historical contexts (pre 1945, communist and post communist) will be examined. Each period comprises an analysis of the change in four institutional variables (the mode of access, the benefit structure, the management of the system and the financing mechanism<sup>5</sup>), as well of the main welfare reform trajectories. The aim here is to highlight the main features that constitute the basis for a correct understanding of current welfare state developments.

### **Economic and Political Situation**

The collapse of the Iron Curtain coincided not only with a new wave of democratization in Europe (Huntington 1991), but also with the emergence of mass unemployment and the consequent rise in poverty and income inequality (see, for instance, Nesporova 2002, European Commission 2004, UNECE 2004, Alam et al. 2005). Just to quote few examples of the difficult socio-economic situation that the four Vizégrad countries faced, and are still facing, real GDP growth reached 1989's levels only in Poland by the mid 1990s, but not before the beginning of 2000 in Czech Republic, Hungary and Slovakia. Inflation, which remained constantly high during the entire period of transition, drastically reduced the purchase power of households. Hungary and Poland were the countries that suffered more with an average annual inflation rate running between 20% and 30% during the first five years and about 10% afterwards. The annual inflation rate in the Czech and Slovak Republics, however, stabilized under the threshold of about 10% only in the second half of the 1990s. Similarly, the employment ratios decreased between 1989 and 2000, from 87% to 71% in Czech Republic, from 83% to 63% in Hungary, from 75% to 62% in Poland and from 80% to 57% in Slovakia (TransMonee 2005). In 2005 GDP per

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<sup>5</sup> As conceptualized by Bonoli and Palier (1998, 2001 p.59), these four institutional variables, more or less, correspond to four main principles (1) the rules and criteria governing eligibility and entitlement: who is entitled to the benefit?; (2) the forms taken by the benefits: what types of benefits are provided?; (3) financing systems: who pays and how?; and (4) the organization and management of the scheme: who decides and who manages? (quoted in Background Paper of the Project, pp. 5-6).

capita in PPs<sup>6</sup> (EU25=100) remains between half and two-thirds<sup>7</sup> of the EU15<sup>8</sup> average, while the total employment rate is equal to the EU15 average (65%) only in the Czech Republic, but substantially lower in Poland (53%), Hungary (57%), and Slovakia (58%). The unemployment rate, which is now close to the EU15 average (7.9%) in Czech Republic (7.9%) and Hungary (7.2%), remains dramatically high in Poland (17.7%) and Slovakia (16.4%). Similarly, the number of people at risk of poverty, raised especially during the first years of transition, is now below the EU15 average of 15% in the Czech Republic (8%) and Hungary (12%), but still higher in Poland (17%) and Slovakia (21%) (Eurostat 2006). In plain numbers, these percentages correspond to 800 thousand people at risk of poverty in Czech Republic, 1.2 million in Hungary, 6.5 million in Poland and 1.1 million in Slovakia (Cerami 2006a, p.18).

Under these conditions of economic instability, it comes as no surprise that the voting behaviour of Central and Eastern European citizens has been greatly influenced by the economic situation of the country. Countries that have faced greater economic instability have also witnessed greater political instability (see Table 1). In the Czech Republic, the Klaus governments have not been reconfirmed in the elections of 1998 and 2002 due to the persistence of the economic crisis, which has delegitimized his reform path. In Hungary, centre-right and centre-left coalitions have both paid high costs for the painful reforms implemented. For example, the centre-right coalition under Prime Minister József Antall (Hungarian Democratic Forum, MDF) was not reconfirmed in the elections of 1994 for having advocated the necessity of introducing a market-economy in the fastest possible way, the elected centre-left coalition (1994-1998) under the leadership of Gyula Horn (Hungarian Socialist Party, MSZP) after having attempted to introduce a set of austerity measures in 1995 (the so-called *Bokros-package*), and the FIDESZ-MPP (Alliance of Young Democrats-Hungarian Civic Party) led government coalition of Viktor Orbán (1998-2002) for having pursued cuts in protection against unemployment policies. Similarly in Poland, from the date of the first totally free parliamentary elections of 1991, centre-right and centre-left coalitions have not succeeded in lasting for more than one legislative term due to the persistence of a severe economic crisis. The unexpected change in voting behaviour, following the introduction of the *Balcerowicz Plan* in 1990, that saw the re-elections of the ex-communists only few years after the fall of the Berlin Wall, is probably the most emblematic example of how the electoral results in the region have been linked to the economic performance of the country. The political survival of Vladimir Mečiar in

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<sup>6</sup> GDP per capita in Purchasing Power Standards (PPS), (EU-25 = 100).

<sup>7</sup> In 2005, GDP per capita in PPs (EU 25=100) was equal to 73 in the Czech Republic, 62 in Hungary, 50 in Poland and to 55 in Slovakia, against an average of 108 in the EU 15 (Eurostat 2006).

<sup>8</sup> The EU-15 includes Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden, and the United Kingdom.

Slovakia was also made possible thanks to the violent political debate that the nationalist Slovak leader conducted in the media accusing Václav Klaus with his neo-liberal reform plan of being the enemy of the Slovak citizens.

<b>Table 1 Elections in Czech Republic, Hungary, Poland and Slovakia (1989-2006)</b>			
<b>Czech Republic</b>	<b>Hungary</b>	<b>Poland</b>	<b>Slovak Republic</b>
Czechoslovakia:	1988 Round Table	1989 Round Table	Czechoslovakia:
1989 Federal Assembly	1990 centre-right (MDF-led coalition)	1989 centre-right (Solidarity-led coalition) semi-free elections	1989 Federal Assembly
1990 centre-right (CF/VPN)	1994 centre-left (MSZP-led coalition)	1991 centre-right (Solidarity-led coalition)	1990 centre-right (CF/VPN)
1992 centre-right (ODS/HZDS)	1998 centre-right (FIDESZ-MPP led coalition)	1993 centre-left (SLD-led coalition)	1992 centre-right (ODS/HZDS)
1993 Dissolution of Czechoslovakia	2002 centre-left (MSZP-led coalition)	1997 centre-right (Solidarity-led coalition)	1993 Dissolution of Czechoslovakia
Czech Republic:	2006 centre-left (MSZP-led coalition)	2001 centre-left (SLD-led coalition)	Slovak Republic:
1993 centre-right (ODS-led coalition)		2005 right-nationalist (PiS-led coalition)	1993 nationalist (HZDS-led coalition)
1998 centre-left (ČSSD-led coalition)			1994 nationalist (HZDS-led coalition)
2002 centre-left (ČSSD-led coalition)			1998 centre-right (KDH-led coalition)
			2002 centre-right (SKDU-led coalition)
			2006 new elections 17.06.2006

Source: Cerami 2005, pp. 13-17; Parties and Elections in Europe : <http://www.parties-and-elections.de/> Czech Social Democratic Party (ČSSD), Civic Forum (CF), Public against Violence (VPN), Civic Democratic Party (ODS), Hungarian Democratic Forum (MDF), Hungarian Socialist Party (MSZP), Alliance of Young Democrats-Hungarian Civic Party (FIDESZ-MPP), Democratic Left Alliance (SLD), Law and Justice (PiS), Movement for a Democratic Slovakia (HZDS), Christian Democratic Movement (KDH), Slovak Democratic and Christian Union (SKDU).

### **Policy Discourses and International Organizations**

Numerous studies have often emphasized the crucial role played by international organizations in influencing the post-communist social policy reform process (Deacon et al. 1997; Orenstein 1998, 2005; Müller 1999, 2002, 2004; Manning 2004; Cerami 2005). The most common approach to welfare state transformation in the region sees, in fact, international organizations as extremely successful in influencing the policy direction through *binding directives* or through forms of *moral suasion*. Examples of binding directives can be found in the World Bank and the IMF's conditionality strategy for

granting access to loans (or in the case of the *Accession Agreements* during the EU Enlargement process), while an example of *moral suasion* can be found in the OECD's *Economic Surveys* (McBride and Russel 2001) or in the EU policy evaluation reviews with their attempt to show governments what good policy-making should look like.

*Policy discourses* (see Schmidt 2000, 2002), promoted by international organizations have, undoubtedly, influenced national policy-making by increasing trans-national communication and thus convergence to already identified policy priorities. In the case of the World Bank and the IMF, the policy discourse has primarily focused on the need for a market-oriented, financially stable and residual welfare state. The EU, on the other hand, has been influential not only in cognitive terms (Guillén and Álvarez 2004; Guillén and Palier 2004; Ferge and Juhász 2004; Lendvai 2004, 2005; Manning 2006), increasing, for example, trans-national solidarity and mutual learning, but it has also been a vital actor in facilitating the introduction of new social policy ideas, interests and institutions (Cerami 2006b). The new social policy ideas introduced by the EU have coincided with keywords such as *activation* in the labour market (see also Clasen 2000), *sustainability* and *adequacy* in the pension sector, as well as *sustainability*, *accessibility* and *high quality* in the health and long-term care sector. Here, the focus has been put not only in the financial sustainability of the system as promoted by most financial institutions, but also in its adequacy, quality and accessibility (see Mandin and Palier 2002 for France). The introduction of these new social policy ideas has inevitably resulted in the formation of new interest-based relations. These have included, for example, the development of strategic interactions and bargaining activities between the various Ministries of Finance, of Social Affairs and the new pension, health care and social insurance funds. Neither ideas could be heard nor interests could have been expressed if the necessary institutions would not have been in place. These institutions have included, for instance, those administrations related to the management and monitoring activities of the new social policy organization at national, regional and local level (such as new ministerial departments or social insurance agencies, and their regional and local offices).

Here, it should be remembered, however, that even the most convincing discourses tend to be mediated in their acceptance by the individual's own preferences. Transformation in Central and Eastern Europe has, in fact, not been simply the result of silent or semi-silent acceptance of prescriptions respectively through *policy transfer* or *policy diffusion*<sup>9</sup>, but rather as a result of a *recombinant policy implementation*, in which existing institutional structures have constrained and/or fostered the full completion of reforms.

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<sup>9</sup> For the most recent debate on *policy transfer*, *policy diffusion* and *policy convergence*, see the special edition of the *Journal of European Public Policy*, Volume 12, Number 5 / October 2005.

In fact, it should not be forgotten that the introduction of a welfare state based on professional diversity and private arrangements was not only the most suitable scheme if the historical background of these countries is taken into account, but it also corresponded to the functional necessity of occupational and market diversification, which stemmed from the excessive centralized and homogenized economic system in force during communism. In this context, it is not surprising that more than ten years after the first attempts of the World Bank to see its policy prescriptions fully and successfully implemented, its Operations Evaluation Department (OED) desolately concluded that more attention to the existing institutional and administrative capabilities of the countries should have been given in order to ensure a more consistent policy execution (World Bank -OED- 2004).

In attempting to assess the real impact on national policy making, it must certainly be remembered that international organizations have been important *facilitators* (Ekiert 2003; Inglot 2003, p. 242; O'Connor 2005) in the social policy reform process, but this is still not sufficient to address them as the only causes responsible for specific outcomes. The presence of social insurance institutions still based on the professional activity, even though encapsulated in the central planned economy, inevitably influenced further reform options of the Vizégrad countries. As it will be shown in the following sections, the reinforcement of schemes based on the payment of contributions and on the professional record of workers was the natural option of a system which previously worked on full-employment, as well as the establishment of social insurance funds was the natural option on the side of the management and financing mechanism, which, in reality, never disappeared from the scene but continued within the state budget. Once the communist state collapsed and with it, numerous enterprises, the organs responsible for proofing and managing the benefits had to be replaced in order to ensure the survival of welfare institutions. Clearly, the market was the only available option and with the market strengthening the importance of independent social insurance funds became unavoidable.

In addition, despite strong pressures from international financial institutions, policy recommendations have tended to be mediated and negotiated in the political arena, according to clear institutional rules, instead of having been implemented by design. Just to quote few but notable examples. The introduction of the three pillar-scheme in Poland, proposed by the Minister of Finance Grzegorz Kołodko, was blocked for two years by the opposition from the Minister of Labour and Social Policy Leszek Miller. The decision of Miller was moved by his commitment to the PAYG principle and by his personal rivalry with Kołodko (quoted in Nelson 2001, p. 244). In Hungary and Slovakia, the introduction of the three-pillar scheme was also subjected to several discussions among politicians

and social policy experts and only at the end of a difficult process of political bargaining was finally introduced. In the Czech Republic, by contrast, agreement on the three-pillar scheme was not found primarily due to the strong opposition by the trade unions (Fultz 2002).

## **1. The Period Before 1945**

### **1.1 Institutional Background**

Until 1918, the territories now comprising the Czech and Slovak Republic were part of the Austro-Hungarian Empire. Hungary, occupied by the Ottoman empire for 150 years, gained independence from the Turks in 1686, but became immediately afterwards part of the Austro-Hungarian monarchy until its independence in 1920. Over a period of several hundred years, Poland was under the foreign domination of Russia, Austria, and Prussia, and whose governments greatly influenced its internal organization after independence. In fact, during the period immediately antecedent the end of World War II, the four Vizégrad countries remained continuously subjected to the regulations and administration of the occupying forces, which greatly modelled not only the character and the borders of these nation states, but also their social security system implemented according to Bismarck principles.

A brief overview of pre-communist pension systems shows, for example, that these countries had already established some form of Bismarck-style pension insurance, which linked the access to benefits to professional status. This link was particularly strong in the Czech Republic and the now independent Slovak Republic<sup>10</sup>, in Hungary<sup>11</sup> and in Poland<sup>12</sup>. In the years 1906 to 1933, the numerous funded pension schemes established were based on a corporatist vision of social solidarity, primarily aiming to secure occupational standards. Health care was also provided on the basis of the professional activity and financed primarily through social insurance contributions. In Czech Republic and Slovakia, the first health policy was introduced in 1918, when the Czech Lands declared their independence from the Austro-Hungarian Empire. The first fully functional health insurance system, however, came into force in 1924 with the adoption of the Health Insurance Act, which provided coverage for employees, approximately one-third of the total population. Hungary emanated the first act on public health in 1876 (Act XIV of 1876). According to the law, the eligible poor obtained free health care at special surgeries. Corporatist social insurance was the foundation of the system. Health care was delivered through the private sector and in some state hospitals. Poland, which has a long tradition of Bismarck social insurance, dates the first legislation back to 1918. This

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<sup>10</sup> Law of 1906 for salaried employees and Law of 1924 for wage earners.

<sup>11</sup> Law of 1912 and Law of 1928.

<sup>12</sup> Law of 1927 for salaried employees and Law of 1933 for wage earners

system provided, however, very limited coverage with only seven per cent of the population insured.

The benefit structure also clearly reflected a Bismarckian orientation. As mentioned, pension and health care benefits were associated to the employees' insurance record and aimed at reproducing the professional achievements. Pension benefits were earnings-related, while the access to health care services, obtainable in public as well as in private practices, depended on the payment of health insurance premiums or, when not available, by payments in cash. This system was highly non-egalitarian and a significant segment of the population remained uninsured.

The management of the social security system was fairly decentralized. The responsibility for old-age and health care protection was primarily given to local communities or workers' associations, which had the duty to ensure a minimum level of subsistence (rather than a minimum living standard) to their members. State intervention in workers' life was minimal and primarily relegated to resolve workers' disputes. The increasing internal tensions caused by the very low living standards of factory workers and agrarians associated to the possible spread of socialist ideals forced the governments of these countries to adopt the strategy developed by Bismarck. The maintenance of social peace was then linked to the introduction of occupational based schemes, in which central authorities had only limited regulatory powers (primarily legislative rather than of supervision).

The main financing mechanism was social insurance contributions, which aimed at covering individuals primarily against the risks associated with old-age and health. There was a basic social safety net for the poor, sponsored by the state or by charity organizations, but this net did not aim at guaranteeing minimum living standards, but rather temporarily aimed to alleviate extreme poverty.

## **2. The Period from 1945 to 1989**

### **2.1 Economic System, Welfare State, Political Institutions and Interest Representation during Communism**

Forty years of Soviet occupation had a huge impact on the past and current Central and Eastern European political, economic and social structure, with important repercussions on the economic organization of the countries subjected to Russian domination, the political and welfare institutions introduced, the profile and responses of governments as well as the structure of organized interests. The central planned economy regulated all spheres of social life. This was a highly centralized system of resource production and

allocation. As Kornai described (Kornai 1980), Central and Eastern European economies were “economies of shortage”, which preferred scarcity of products to inflation. Policy-makers developed five years plans in which the economic priorities and objectives of the country were identified and pursued (Kornai 1992). Unfortunately, the information required for the complex mathematical calculations was insufficient or simply not available and the final result was poor economic performance.

The welfare state was part of the central planned economy and built on a mix of corporatism and universalism. The Soviet-style economies were based on full-employment and this ensured that the corporatist basis of the system achieved universal coverage (see also Standing 1996). Pensions, for example, were based on contributions and, in theory, linked to the professional status, but the equalization of wages as part of the communist ideology, transformed contribution-related into flat-rate benefits. Health care was granted free of charge and provided under the so-called Semashko model. This was a centralized system of health care planning and distribution, with decisions primarily taken at the national level, rather than by local administrations (Kornai 2001). Family benefits were extensive and primarily aimed at consecrating the role of women as wives-mothers-workers<sup>13</sup>, rather than to ensure a fully gender neutral society.

Serious structural economic problems, however, did exist. The Soviet Union had delegated to each country a specific economic task, favouring mono-sectoral to multi-sectoral productive activities (Bafoil forthcoming). This had the obvious result of making the countries dependent on the import of goods. Despite the mass shift from agrarian to industrial societies, cross-national differences persisted among the four Visegrad countries during the entire period of Soviet occupation. In the Czech part of the Czechoslovakia, for example, the industrial sector was more developed than in the Slovak side, which, in turn, still presented several deficiencies typical of an agrarian society. Farmers were also an important group in Hungary and in Poland, even though the presence and significance of industries incessantly grew during the 1950s, 1960s and 1970s (Adamski et al. 2001; Machonin et al. 2001; Spéder et al. 2001; Tuček 2001; György and Róbert 2003).

As far as political institutions and the associated interest representation is concerned, the four Visegrad countries inherited a highly centralized and totalitarian political structure (Glaeßner 1994), which was only drastically reformed in 1989. As already known, the communist system was a one-party system. The politbüro was the centre of the political

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<sup>13</sup> On the role of women as wives-mothers-workers, see Makkai (1994), Paci (2002), Pascall and Manning (2000), Fodor et al. (2002), Fultz and Steinhilber (2003), Manning (2004), Cerami (2005), Pascall and Kwak (2005).

decision-making and from the politbüro the communist nomenklatura also decided the economic priorities of the centralized country. No federal state was allowed during communism, since this may have represented a threat to the Soviet domination. Hence, no regional requests could be expressed or heard<sup>14</sup>. With regard to interest representation, despite the presence of special privileges to particular professional groups (such as miners, police, or armed forces) (Bafail forthcoming), only the trade unions officially attached to the communist party were allowed in the political arena and, as a consequence, they represented the interests of the communist leaders rather than the interests of workers<sup>15</sup>. To use Hirschman's (1970) terminology, in the communist system, no real *voice* or *exit* options were possible, but only *loyalty* (or rather *forced loyalty*) to the state apparatus was accepted.

The totalitarian political system and the absence of an open structure of interest representation had also several negative repercussions in the private life of citizens. Since voices could neither be expressed nor heard, anomy and apathy among citizens were the norm. This resulted in servility (or forced servility) of the individuals to state organs as well as to the formation of a dual personality (Szalai 2005a). Central and Eastern European societies were, as a consequence, atomized societies, where people searched refuge in the private life, trying to develop "connections" (e.g. with the mayor of the city or the manager of their enterprise) in order to have access to a better life on an individual and private basis, rather than openly according to well defined rules in the public sphere.

The existence of a monolithic structure of power, however, does not mean that changes in the system, even small, could not occur. The centralized political institutions, in fact, were forced gradually to deal with the increasing aspirations in decision-making of the peripheral zones, especially present in Hungary and Poland. It is also questionable whether only one economic system existed during communism. In Hungary, for example, Hankiss (1991) and many others have spoken about the existence of a second economy, where the emergence of small private businesses was tolerated by the communist leaders in order to compensate citizens for the shortages of the official economic system. The existence of a second economy also led other authors to talk about the slow emergence of a "second society" within the official communist one (Ettrich 2003; King and Szélenyi 2004; Szalai 2005a). This was not only the case of Hungary, but also of Poland and, to a lesser extent, due to its industrial character, of the Czechoslovakia. The

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<sup>14</sup> Requests for a federal state, however, existed and were particularly strong in Czechoslovakia (Vodička 2005).

<sup>15</sup> In many large state-owned enterprises, there were also special offices ruled by the secret police which had the function of listening for voices of dissent in the factory and immediately re-establishing the order (Bafail forthcoming).

emergence of alternative forms of interest representation did not only emerge within this second economic sub-system, but could also slowly be witnessed in the public scene. The circles of dissidents and intellectuals in Hungary (see Konrad and Szélenyi 1978; King and Szélenyi 2004), the civic movement Charta 77 in Czechoslovakia or the trade union Solidarnosch in Poland are few but notable examples of the disintegrating tendencies that grew within the communist system.

## **2.2 The “Golden Age” of Central and Eastern Europe**

The years from 1950s to 1970s are usually defined the “Golden Age” of Western European welfare states, whose main characteristics were a rapid increase in welfare expenditures, but also, and more importantly, a rapid expansion in entitlement and eligibility criteria for accessing benefits. Did the *golden age* of Western European welfare states coincide with the *golden age* of Eastern Europe? Even though it might seem implausible due to the huge differences present in the economic structures of the two societies, the two golden ages practically coincide, and also for similar reasons. As Szalai (2005a) has pointed out, Western European nations were not alone in the world and all of them were confronted with the social, economic and technological achievements of their, at the time, enemies of the Warsaw Pact. Similarly, Central and Eastern European societies were not immune to the cultural, political and social achievements of Western societies, but were forced to deal with their, at the time, corrupt *alter ego*. The development of an extensive welfare state in Europe able to ensure universal coverage for the citizens should, in fact, be explained not only in terms of class struggles as the *power resource model* would suggest (see Korpi 1983, Esping-Andersen 1985; Baldwin 1990), or as a result of deindustrialization (Iversen 2005) or again as the consequence of increasing global economic competition (Rieger and Leibfried 2003), but also as an outcome of the strategy of confrontation during the Cold War.

The process of modernization in Central and Eastern Europe, started with the development of heavy industry in the 1950s, which resulted in an extraordinary increase in living standards. These, however, were maintained artificially high, for political and propaganda purposes, beyond the real possibilities of the central planned economy. The artificial raise in living conditions through various state subsidies coupled with a constant increase in military expenses put the productive and distributive capacities of the central planned economy under great financial pressure. Constructing an always larger number of nuclear missiles, submarines, or engaging in the “space race” with the United States were extremely expensive political exercises that, in some way, had to be financed. Funds could only be raised at this point either from a reduction in expenditures for those policies indirectly aimed at subsidizing the economy and, hence, at raising living

standards (such as price subsidies or subvention to modernize the firms) or, as last resort, from an increase in external debt. The latter option was the one preferred by almost all countries. By 1989, for example, the gross convertible external debt reached USD 7.9 thousand million in Czechoslovakia, USD 19.2 thousand million in Hungary, and USD 40.8 thousand million in Poland (Szalai 2005a, p. 32).

Nevertheless, by the end of the 1980s, the welfare state, which was continuously expanding<sup>16</sup>, financed through external debt, was no longer able to ensure the social stability it had ensured previously after the attempts of revolt in Budapest in 1956, after the *Prague Spring* in 1968 and in Poland in the early 1980s. These were, in fact, not only the years where the communist system vacillated due to mass demonstrations, but also the years in which political leaders consolidated their power through an expansion in welfare provisions (Szalai 2005a). The establishment of an extensive welfare state was, thus, the reward that Eastern citizens received in exchange for their liberty, whereas the institutionalization of welfare rights, that had radically increased during the 1960s and 1970s, functioned in legitimizing the political system introduced by dictatorship. Despite increased attempts to increase the distributive possibilities of the central planned economy, already grown to limits through external funding, the dissatisfaction among citizens, already high, grew, leading to the collapse of the system on 9 November 1989, day of the fall of the Berlin Wall.

### **2.3 Welfare Reform Trajectories before the Fall of Communism**

At first glance, the primary characteristic of contemporary Central and Eastern European systems of social protection is the implementation of third order (or paradigmatic) changes, since a simultaneous transformation in all the components of policy (the instrument settings, the instruments themselves, and hierarchy of goals behind policy) (Hall 1993, Palier 2000, Bonoli and Palier 2001) seems to have only occurred since 1989. A new benefit system, new modes of entitlement and calculation for retirement, unemployment, health, family and social assistance provisions have been introduced under a new welfare logic, which aimed at conducting a shift from the communist state-paternalism to a market-oriented welfare state, based, if still not on individual, then at least on semi-individual responsibility. However, it is important to remember that first and second order changes were already initiated before 1989.

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<sup>16</sup> Please note that it would be impossible to analyze social security expenditures in CEE without considering other "indirect social policies" such as job security, price subsidies, subvention to firms, to house, education, etc. In fact, as Simpura (1994, p.150) has emphasized, all policies were "social" by definition during communism.

In the Czech and Slovak Republic, the labour code dates back to 1965<sup>17</sup> and has been used as the reference text for current legislation on labour and employment. Similar considerations apply to labour inspection and labour safety<sup>18</sup>, to maternity leave, maternity benefits and children's allowances<sup>19</sup>, medical care and sickness benefits<sup>20</sup>, and to pensions<sup>21</sup> (ILO 2005, Natlex Database). The mass demonstrations in 1968, however, did not lead to a faster implementation of reforms, as in Hungary after the protests in 1956 and in Poland in the early 1980s, but rather to a welfare state reorganization anchored in the communist orthodoxy. In fact, after the *Prague Spring*, the Czech Republic went through the so-called process of "normalization", which involved not only the re-introduction of old political rules, but it also coincided with the dismissal of numerous party officials, managers, academics and journalists. The economic, political and scientific elite was soon replaced with persons more loyal to the communist system. The then reforms in the social security system recently introduced as part of the reform package of Alexander Dubček were temporarily frozen. "Normalization" in the welfare state primarily involved the attempts of decentralization of tasks and responsibilities under the federal reform proposal, which would have inevitably meant an increase in local authority over the management of the social security system, but also attempts at differentiating the access and entitlements to pensions, health care and family benefits.

In Hungary, several modifications to the communist style social security system took place, since the end of 1960s, involving medical care and sickness benefit<sup>22</sup>, pensions<sup>23</sup>,

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<sup>17</sup> Labour Code No. 65/1 of 1965 regulated the workers' relations.

<sup>18</sup> Act No. 174 of 1968 on State Inspection of Labour Safety. It regulated the rights, functions and competencies of labour inspection bodies.

<sup>19</sup> Act No. 88/1968 on maternity protection. It concerned the extension and new entitlement criteria for maternity leave, maternity benefits and children's allowances.

<sup>20</sup> Act No. 54/1956 on employees' sickness insurance.

<sup>21</sup> Several modifications concerning pension benefits, entitlements and social insurance contributions occurred since 1960s. A detailed list is provided by Mrázová et al. (2004).

<sup>22</sup> Act No. II of 1975 on social insurance (with later amendments).

<sup>23</sup> Act No. II of 1975 on social insurance (with later amendments); see also Ordinance No. 1 of 1971 of the Ministry of Health with respect to yearly increases in old-age pensions; Regulation No. 6 of 1970 of the National Council of Trade Unions on mutual old-age pension insurance for agricultural co-operative workers; Government Ordinance No. 18 of 1969 on compulsory retirement pension insurance for handicraft; Decree No. 42 of 31 December 1969 on the introduction of compulsory old-age pension insurance in private commerce; Regulation No. 12 of 1968 of the National Council of Trade Unions on the amount of old-age, disability and survivors' benefits for rural workers granted on the basis of the length of their membership of rural cooperatives.

employment<sup>24</sup>, social assistance<sup>25</sup>, equality between men and women<sup>26</sup>, as well as the social security general standards<sup>27</sup> (ILO 2005, Natlex Database). Here, due to the introduction of the New Economic Mechanism (NEM) in 1968, Bismarckian principles, such as differentiation of access and provisions, were more easily pursued than in Czechoslovakia. "Goulash Communism", the particular Hungarian way between market and socialism, introduced by the Kádár government in order to pacify the requests of the population humiliated by the repression of 1956, had obvious repercussions in the social security system. These repercussions involved not only universal extensions in the pension and family benefit sector (Ferge 1979; Szalai 2005a), but also the indirect acceptance of principles based on differentiation of provisions, professional activity and contribution records. In the late 1980s, due to serious fiscal crisis, Hungary decided to separate the social security fund from the state budget, thus differentiating pensions, family benefits, sickness, maternity and other social security payments (Müller 1999; Inglot 2003, p.221)

Similarly in Poland, the reform of the communist-style welfare state began in the early 1960s and concerned all spheres of the social security system, including the general

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<sup>24</sup> Labour Code of 1967 regulated the workers' relations; see also Ordinance No. 2 of 1970 on respecting the employment of younger workers; Ordinance No. 8 of 1970 of the Minister of Labour on respecting the settlement of labour disputes (with later amendments); Act No. II of 1975 on social insurance (with later amendments); Decree No. 20 of 1979 of the Ministry of Labour on respecting collective bargaining; Decree No. 10 of 1981 on respecting the protection of labour.

<sup>25</sup> Decree No. 9 and No. 18 of 1979 of the Minister of Labour on social and cultural benefits.

<sup>26</sup> Government Ordinance No. 16 of 1966 on family allowances (with later amendments); Government Order No. 103 of 1970 on the improvement of the economic and social condition of women; Act No. II of 1975 on social insurance (with later amendments); Decree No. 6 of 1982 of the Ministry of Health on protection of the health of women and young children.

<sup>27</sup> Act No. II of 1975 on social insurance (with later amendments).

standards<sup>28</sup>, pensions<sup>29</sup>, medical care and sickness benefit<sup>30</sup>, maternity<sup>31</sup> and employment<sup>32</sup> (ILO 2005, Natlex Database). The 1970s workers' demonstration under the Gierek regime opened the door for heavy occupational lobbies (Inglot 1994, 2003, p.220), notably the requests of farmers for an extension in pension and health insurance, while the presence of the strong trade union *Solidarity*, particularly active in the early 1980s, allowed an increase in the requests of industrial workers exacerbated by the continuous deterioration of their life and working conditions. Inglot (2003, p. 220) noticed, for instance, that during the crisis of 1980-1982 the share of cash benefits in overall social spending unexpectedly jumped from 47 to 57 percent. Interestingly, in 1987, two years before the collapse of communism, the Jaruzelski government also decided to separate the Social Insurance Fund from the state budget (Inglot 2003, p. 221), concluding the reform attempts initiated some decade before.

#### **2.4 The Four Institutional Variables**

Following the Soviet occupation after World War II, the dominant Bismarckian mode of access to benefits was not completely abolished by the communist regime, but rather it was expanded in order to bring it in line with the egalitarian aspirations of the Bolshevik revolution. Here, it is important to point out that the communist understanding of citizenship coincided with the idea of the perfect communist worker (such as Stakanov). Every citizen had the right and obligation to work not only for the sustenance of his or her family, but also for the economic development of the country (Ferge 1979). As a consequence, welfare rights and entitlements continued to be based on the professional activity, but the corporatist orientation was covered up by the egalitarian communist

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<sup>28</sup> Order of the Council of Ministers concerning workers' rights to social security contributions (Text No. 211 of 1987); Act on respecting the organization and financing of social security, including social insurance contributions (Text 202 of 1986); Order of the Council of Ministers on the organization and rules of the Social Insurance Institution.

<sup>29</sup> Act on retirement pension schemes for workers and their families (Text No. 267 of 1982) with later amendments; Act respecting the organization and financing of social security including social insurance contributions (Text No. 202 of 1986); Decision No. 142 of 1986 of the Council of Ministers on periods of employment necessary to pension security; several decrees and government orders concerning remuneration and entitlements of benefits since the end of 1960s.

<sup>30</sup> Act on cash social insurance benefits (Text 185 of 1975) with later amendments; Act on retirement pension schemes for workers and their families (Text No. 267 of 1982) with later amendments; Order of the Minister of Labour, Wages and Social Affairs on the calculation of social security allowances (Text 336 of 1974).

<sup>31</sup> Decision No. 58 of the Council of Ministers on unpaid leave for working mothers with children (Text 154 of 1968); Order of the Minister of Labour, Wages and Social Affairs on the calculation of social security allowances in the event of sickness and maternity (Text 336 of 1974).

<sup>32</sup> Labour Code of 26 June 1974 with several amendments; Act on State Employment Fund (Text 334 of 1983) first establishment in 1974 (Decision No. 44 of the Council of Ministers); Decision of the Council of State respecting the registration of the newly established trade unions (Text 104 of 1980); Act on respecting trade unions (Text 212 of 1982).

propaganda and by the fact that there was practically no unemployment. Clearly, things went differently for those minorities, who were, for some reason, outside of the labour market (such as Roma, pensioners, handicapped). In this case, the universal and egalitarian aspirations of the communist regime faced a drastic slowdown. Poverty and, what nowadays we would call, social exclusion were associated with an implicit social stigma. In the eyes of the many citizens that regularly took part in the economic, social and political life, being the beneficiary of some form of social assistance benefit (in-kind or in-cash) was inevitably the result of a reactionary or, in the worst case, of a counter-revolutionary behaviour (Milanovic 1995; Cerami 2005).

With the introduction of the central planned economy, the benefit structure was equalized. Flat-rate rather than contributory benefits became the new characteristics of the pension system, while universal and standardized treatments were the norm in public, state-run hospitals. Unfortunately, the egalitarian aspirations of the communist nomenclature did not coincide with a positive performance of welfare institutions. A poor working life was usually followed by a poor retirement (Connor 1997), while health care services were highly inefficient and characterized by high morbidity rates (Deacon 2000).

The extremely differentiated schemes established during the Bismarckian period in Eastern Europe were put under the control of central authorities, with social insurance revenues and expenditures becoming integral part of the central planned economy. Social insurance contributions, which persisted in these countries even during the 1970s, were transferred to the state budget (or in funds within the state budget) and, subsequently, redistributed to the entire population. The management of the social protection system was highly hierarchical and based on a top-down approach. The Ministry of Social Affairs (or Health) planned the relative policies. These were then implemented by local authorities on the basis of the decisions and the national priorities taken at the central level, often with little or no knowledge of local real needs. Trade unions were also in charge of social insurance administration, but since only the official communist trade union was allowed, the independence from state authority was extremely limited. The access to welfare benefits, by contrast, followed a bottom-up direction and was characterized by a high degree of discretion of those officials who were responsible to grant the benefits. In order to get access to welfare provisions (such as pensions, maternity leaves, etc.), state-factory workers usually informed (or asked the permission of) their supervisors at the work place, who then gave the request to the state-factory managers. These finally gave the consensus on the access of benefits<sup>33</sup>. A

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<sup>33</sup> The main argument for the management of social policies at the firm level was based on the assumption that this kind of decentralization would have been helpful to better meet local needs, if compared to the low administrative capabilities of central public administrations. Moreover, the allocation of resources was also

clientelist access to welfare provisions soon became a normal praxis, and is of particular interest for the understanding of current social policy developments. Loyalty to the state apparatus in exchange for short- and long-term benefits (such as better jobs, longer holidays, better houses, access to prestigious schools and universities) created circles of clientele around local party officials and administrators that tend to persist even to the present day<sup>34</sup>.

Although state participation in the financing of the communist welfare state was greatly enlarged, social insurance contributions did not completely disappear from the scene. While in Czechoslovakia, social insurance premiums were automatically included in the state budget<sup>35</sup>, in Hungary and Poland they were still considered to be a separate part of social security receipts. As Table 2 shows, during the period from the 1960s to the end of the 1980s, the receipts from employers' contributions in Hungary were equal or higher than state participation receipts, while the contributions paid by the insured corresponded to approximately one-fifth (slightly below 20%) of total social security revenues. In Poland, the largest part of total social security receipts was paid through employers' contributions, which remained constantly higher than the receipt coming from state participation, and that covered the low revenues of insured premiums.

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supposed to be just among workers, who, according to the communist propaganda, were at the same time employees and owners of the state factories. This kind of arrangement should then have helped to improve the productivity of workers (Ferge 1979).

<sup>34</sup> Interview with ILO-SRO Expert, Budapest, 30 July 2002: "One of the important problems regarding the socialist social security heritage is the continuation of forms of patronage [The interviewer suggests the word "clientelism". We both agree on that]. During socialism, for instance, the state companies controlled everything. [Interviewer: Yes, I know, being manager of a state company meant deciding who gets benefits and under what circumstances. But, now, most of these actors are changed. Being a member of the communist party is no more a determinant factor]. Yes, but forms of "clientelism" are still in place. An example is the existence of "gratitude money" in the health care sector.

<sup>35</sup> This was probably a reaction of the communist government to the *Prague Spring*. In fact, while after the demonstrations in Hungary in 1956 the government responded by making liberal concessions to the populations in exchange for social peace, in Czechoslovakia the response was primarily concerned with re-establishing the communist orthodoxy.

**Table 2. Social Security Receipts: Percentage of Contributions paid by Insured Person, Employers and State Intervention**

Czechoslovakia				Hungary				Poland			
Year	insured	employers	state intervention	Year	insured	employers	state Intervention	Year	insured	employers	state intervention
1963	2	33	65	1963	12	47	42	1963	0	63	37
1966	0	35	65	1966	14	40	46	1966	1	61	38
1971	0	3	97	1971	17	52	31	1971	10	54	36
1974	0	3	97	1974	17	43	40	1974	4	59	37
1977	0	3	97	1977	16	46	38	1977	1	57	42*
1980	0	3	97	1980	14	40	46	1980	2	52	46
1983	0	3	97	1983	15	47	38	1983	3	61	36*
1986	0	4	96	1986	21	79	0	1986	3	61	36*
1989	0	4	96	1991	25*	75	0	1989	2	70	28*
1990	0	4	96					1990	3	68	29*
1993	0	4	96								
1996	0	4	96								
1999	0	4	96								
2000	0	4	96								

Source: ILO/MZES 2001. Author's calculations.

\*Estimated

As Manow and Plümper (2005) have demonstrated, the ways how a welfare state expands may depend on the existing financing structure of welfare institutions (tax vs. social insurance contributions), but also by the degree of freedom of the institutions responsible for monetary policies. In economies based on central planning, as mentioned, the main characteristic was an ambiguous contributions-oriented system that equally redistributed the resources collected, while the institutions responsible for monetary policies were fully subjected to the state authority. It comes then as no surprise that rising contributions also coincided to an increase in an external debt as it happened in countries with a low degree of central bank independence and Bismarckian welfare states such as Belgium, France, Italy, Portugal and Spain (see Manow and Plümper 2005).

### 3. The Period from 1989 onwards

#### 3.1 Welfare Reform Trajectories after Communism

At the beginning of the 1990s, structural reforms were implemented that remained under the dominant Bismarckian logic introduced in the pre-Soviet period and continued even during communism. Welfare benefits granted on the basis of professional activity and according to the work record of individuals continued to be financed through the payment of social insurance contributions, which this time, however, were redistributed, to a lesser extent, among the population in absence of a centrally planned economic mechanism. Professional diversity, differentiation of provisions and privatization of schemes soon became the keywords of the new post-communist consensus. In short, three sequences of reforms can be identified since the collapse of communism: (1)

*forced expansion, (2) attempts at privatization, and (3) re-adjustment* (see Table A.1 in Appendix).

### **3.1.1 First Sequence of Reforms**

The first sequence coincided with the *temporary growth of welfare provisions* called to help the democratic transition of Eastern Europe. The new problem of mass unemployment resulting from the dismissal of workers of state-owned enterprises was first tackled by the introduction of extensive early retirement policies, followed by the establishment of relatively far-reaching unemployment and social assistance programmes (Standing 1996; Kapstein and Madelbaum 1997; Milanovic 1995, 1998; Vodopivec et al. 2003). Vodopivec et al. (2003, p.6) have shown, for example, that these countries have not only spent considerable resources on promoting early retirement (reaching 0.8 percent of GDP in Slovakia in 1992), but also that the replacement rate and the generosity of unemployment benefits decreased only in a second phase of transition.

However, during this phase, not only temporary emergency policies were implemented, but also the first steps for future, long-lasting reforms were taken. The CV/VPN and ODS-led governments in Czech Republic and the HZDS-led government in Slovakia, the MDF and the MSZP-MPP coalitions in Hungary, and the *Solidarity*-led alliances in Poland started, in fact, the first attempts to move away from the old pay-as-go-system, by creating the basis for the future adoption of the three pillar schemes (or private funds in the case of the Czech Republic). This also included the reinforcement of principles based on pension insurance, as well as a slow raise in retirement and contribution rates, which remained set at an extremely low level during the entire communist period (usually 60 years for men and 55 years women, with approximately 25 years of service). In the health care sector, the main characteristics of reforms were the reintroduction of health insurance, a clearer separation in the management and financing the system (from taxation to contributions and from the state budget to separate funds), as well as the establishment of private practice. On unemployment and social assistance, this involved the introduction of unemployment insurance, as well as the establishment of a basic social safety net. Finally, on family benefits, the temporary maintenance of extensive family policies had the aim of cushioning some of the costs of transition, since policy-makers in the region saw family protection as the most effective way to target poor people (Interview no. 2).

### **3.1.2 Second Sequence of Reforms**

Of course, the early generosity soon became unsustainable, especially due to the escalating number of unemployed. The second sequence of reforms, *attempts at*

*privatization*, were introduced in order to reduce the expansion of the welfare state. The measures used to prevent such uncontrollable extension of rights and claims were again primarily rooted in the Bismarckian tradition. These involved, of course, the privatization of provisions, as sponsored by the most influential international financial institutions, as well as also and, perhaps, more importantly, the reinforcement of principles based on professional diversity. A process of *monetarization and individualization of risks and responsibilities* (Ettrich and Cerami forthcoming) was then enclosed in a Bismarckian welfare logic, which saw in the establishment of insurance-related pension, health care and unemployment schemes. This seemed the best way to cut expenditures, while, at the same time, ensuring professional diversity and market orientation. In Hungary, attempts at retrenchments were carried out by Finance Minister Lajos Bokros in 1995, who unsuccessfully tried to introduce a set of austerity measures (the so-called *Bokros package*) with the aim of making family allowance no longer universal and automatic, of conducting a shift from flat-rate to means-tested benefits, of reducing child-care assistance and of introducing the tuition fees for universities. In Czech Republic, the Klaus governments pushed for a drastic reduction in the protection against unemployment policies especially during the second half of the 1990s. Fascinatingly, the policy discourse during these years reached a peak in neo-liberal orientations with some Czech officials affirming that unemployment was something natural and beneficial for the country. If no unemployment would have existed, then something would have been wrong with the country (Consensus II 1999: Czech Republic, Part IV, p.150). In the mid 1990s, a report called *Security through Diversity* also opened a temperamental debate in Poland between the Ministry of Finance and the Ministry of Social Affairs on the incontrovertible necessity of drastic social security reforms. Similarly in Slovakia, violent discussions on the necessity of privatizing health and pensions also took place at about the same time. It is not by chance that most pension and health care reforms (notably the full introduction of the three pillar scheme in Hungary and Poland, and the reinforcement of health insurance principles in Czech and Slovak Republic) took place close to the end of the 1990s. These were, undoubtedly, the years where endogenous and exogenous economic vulnerabilities became stronger and actions were addressed as urgent by the national, as well as by the international, community, but these were also the years where the Bismarckian character of welfare institutions was reinforced on the basis of the country's historical background.

Interestingly, the left/right divide was not a determinant factor for party preferences towards neo-liberal or social democratic reforms. In fact, not only centre-right parties, like the ODS-of Vaclav Klaus in Czech Republic, have opted for welfare cuts, but also left-wing governments, like the MSZP of Gyula Horn in Hungary, or the catholic *Solidarity*

coalitions in Poland<sup>36</sup>. One plausible explanation for the rather unusual behaviour of left-wing parties is the one provided by Müller (1999, 2002, 2004), who sees such reform attempts as driven by the necessity of left governments, on the one hand, to increase their international legitimacy after forty years of communism, while, on the other, to let the population digest more easily the absolutely necessary reforms. Right-wing parties would have not had, in fact, the same moral authority. The *Nixon goes to China Syndrome* (Müller 1999, 2002, 2004) seems, as a consequence, to have characterized the politics of social security reforms of left wing-parties in the first years of transition, even though this does not seem to be the case nowadays (see below).

### 3.1.3 Third Sequence of Reforms

Owing to problems connected with the growing number of unprotected citizens attempting to claim from the already indebted social insurance funds, the excessive optimistic vision of *market-driven change* did not survive its arrival. The third sequence of reforms, strongly characterized by policy learning dynamics (on policy learning see Hemerijck 2005), was that of *recasting* (Ferrera and Rhodes 2000) or *recalibrating* (Pierson 2001) the neo-liberal approach introduced by most Central and Eastern European governments. In Czech Republic, numerous private health insurance funds evaluated as unable to provide minimum standards for their clients have now been abolished, while in Hungary the compulsory affiliation to the second private pillar of pension, once mandatory for younger generations, has been eliminated. In Poland, unemployment benefits still financed by employers' contributions are now granted on a flat-rate rather than on an occupational basis so as to reduce the financial pressure caused by raising unemployment, whereas in Slovakia the full implementation of a strong market-oriented health insurance is facing increasing policy resistance due to the universal requirements expressed by the Slovak Constitution.

How can such change in orientation be explained? Undoubtedly, *blame avoidance* (Pierson 2001) and *credit claiming* (Mayhew 1974) strategies now play a greater role than in the past. Politicians are, in fact, increasingly searching for ambiguous political and policy agreements in order to see their economic and social policy goals implemented, while, at the same time, trying to ensure the continuation of their own political career<sup>37</sup>.

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<sup>36</sup> The *Solidarity* coalitions represented the political wing of the Polish catholic trade union and, as a consequence, should have opted, in a more determined way, for a workers' friendly transformation.

<sup>37</sup> The most emblematic example is provided by the so-called "opposition contract" between the ODS and the ČSSD in the Czech Republic. The pact between the two main leaders, as Vodička (2005, pp. 145-146) explains, was: Miloš Zeman would have renounced his position as Secretary of the ČSSD in order to be elected as candidate *super partes* to the next presidential elections of 2003, while Václav Klaus would have received, in exchange for his support, the position of Prime Minister in the ODS minority-led government. When Zeman appointed Vladimír Špidla as his successor, it was implicit that tolerance for Klaus' economic preferences would

Political leaders staying in the government are also more often claiming responsibility for the “missed disaster”, which would have followed the non-implementation of reforms. Also parties in opposition affirm with more determination responsibility for having avoided even a more painful economic transformation through their blockades in the parliament. The most recent election results in the Vizégrad countries can, perhaps, be used as a good indicator of how the approach of politicians will inevitably tend to be more cautious. In Czech Republic, for example, the ČSSD centre-left coalition was elected in 1998 and reconfirmed in 2002 primarily thanks to its opposition to the neo-liberal reforms proposed by Vaclav Klaus. Klaus was, in fact, famous among the public for advocating a “market democracy without adjectives”, where the adjective was clearly “social”. Similarly, centre-left coalitions in Hungary, guided by the ex-communists of the MSZP, survived not only a political scandal that involved the ex Prime Minister Péter Medgyessy, accused of having been an ex communist spy, but have also been reconfirmed in 2006, this time under the guide of Ferenc Gyurcsány. In Poland, after the introduction of drastic social security reforms in 1998, the *Solidarity* centre-right government was forced to leave the place to a centre-left coalition. In the next elections of 2005, a right-nationalist government, whose main parties have the very telling names of Law and Justice (PiS), Self-Defense of the Republic of Poland (SO) and League of Polish Families (LPR), unexpectedly won the majority in the parliament. Also Slovakia has seen the alternation of various coalitions, even several times within the same legislature, whose main internal conflicts were not only caused by the authoritarian leadership of Vladimir Mečiar, but also by the debate on the most suitable approach for reforms. In this context, it would be no surprise to see that in the next elections of June 2006, the social security reform will play the determinant factor driving the political behaviour of Slovak citizens.

Despite the importance of this actor-centred explanation, the political behaviour of citizens and politicians is still not sufficient to fully understand the path of social security reforms in the Vizégrad countries. The role played by already existing institutions must also be seriously taken into account. As the next paragraph will summarize, reforms in the mode of access, benefit structure, management and financing of the new welfare state was carried out according to two main principles, which were deeply rooted in the communist and pre-communist past. The first principle was driven by the experience of the excessive standardization of economic and social life caused by the regulatory mechanisms of the central planned economy, which produced the undesired effect of limiting work performance in the absence of incentives, stagnation or even regression of

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have been due. Unexpectedly, Špidla, instead of supporting the already existent “opposition contract”, decided on campaigning against the ODS, but he was then subjected to a *coup d’ état* conducted by the members of his own party.

modernization (Machonin 1997). As a result, the aim of politicians and policy-makers was to provide a differentiated socio-economic system in which the personal aspirations of citizens could be better realized. In the areas of social policy, this coincided with the re-introduction of provisions based on occupational diversity, which also had a long tradition in these countries. At the same time, forty years of communism had produced a system of formal and informal norms that made an extremely differentiated access to welfare provisions not a viable political decision. The state paternalist welfare state established during communism could not simply be dismantled overnight, especially in times where the costs of the economic transition would primarily lay on the poorer social classes. The reinforcement of Bismarck institutions, never completely dismantled during communism, was then the most obvious option.

### **3.2 The Four Institutional Variables**

Nowadays, the mode of access to benefits in the four Vizégrad countries is based on the Bismarck model, but significant universal aspirations exist. In the Czech Republic, Hungary, Poland and Slovakia, the access to pensions is regulated by the payment of social insurance contributions, but a strong link to social assistance provisions (the so-called fourth pillar) ensures coverage for those people who, otherwise, would remain uninsured (Wagener 2002; Tomka 2004). The same applies with regards to health care protection. All these countries now grant health services upon the payment of health insurance premiums, but the state is often called to cover the deficit of the newly established health funds and to ensure that numerous unprotected citizens, such as unemployed, students, children, pensioners, and persons in need are covered (Cerami 2005, 2006c).

Though primarily Bismarckian in its character<sup>38</sup>, the benefit structure of current Central and Eastern European welfare institutions can be described as an ambiguous mix of differentiation and equalization of provisions. Just to quote few example, in the Czech Republic, pensions are financed by social insurance contributions and are calculated on the basis of two amounts: (1) a basic flat-rate based on citizenship and (2) an additional earnings-related component based on the professional status. The flat-rate component of pensions plays the role of equalization at the expense of the middle and upper classes (Consensus II 1999; Tomeš 2003; MISSOC 2005). In Hungary, most of health services are included in the mandatory health package, which are covered by the compulsory insurance scheme. As a consequence, there is little space for additional private health care services and because of this the majority of the citizens have access to the same provisions (Gál et al. 2003, p. 78; MISSOC 2005). For Kornai (2001), in fact, the current

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<sup>38</sup> In the four Vizégrad countries, welfare benefits are: (a) primarily financed by social insurance contributions; (b) earnings-related; and (c) granted on the basis of the professional record.

Hungarian health care system still displays some characteristics of “market socialism”. In Poland, unemployment benefits are financed by social insurance contributions, but their amount is now granted on a flat-rate basis. A differentiated welfare system also exists for farmers, who are insured by KRUS (Social Insurance Fund for Farmers) in contrast to ZUS (Social Insurance Institution), which is responsible for employees. In KRUS, pensions are still based on a first pay-as-you-go component (I pillar), while health insurance has higher universal aspirations (MISSCEEC 2002; MISSOC 2005). In Slovakia the aim of the new pension formula is clearly that of encouraging professional diversity, but the system, work-related in scope, has still universal aspirations. Article 39 of the Slovak Constitution affirms the right to adequate material provisions for pensioners establishing a strong linkage with the minimum guaranteed income (MISSCEEC 2002; MISSOC 2005).

In Central and Eastern Europe, decentralization and devolution of responsibilities to regional and local authorities has been the main characteristic of reforms, although some form of re-centralization is observable. Devolution can be explained as a reaction to the communist over-centralization, which had neglected local requests in order to meet national priorities. As it can be seen by the administrative organization, the system is nowadays much more differentiated. In the Czech Republic, Hungary, Poland and Slovakia, the Ministries of Labour and Social Affairs are responsible for planning policies and drawing up legislation for the overall social security system, with the exception of the health care, which is, usually, under the control of the Ministry of Health. Distinct and autonomous bodies (such as the Czech Administration of Social Security, the Hungarian Central Administration of National Pension Insurance, KRUS and ZUS in Poland, or the Slovak Social Insurance Agency) administer the new social insurance system and pay the benefits through their district and local offices. Also the role of trade unions, usually addressed as the *weakest link* in the reforms process (Ghellab and Vaughan-Whitehead 2003), has now drastically increased. Despite common assumptions, tripartite consultations have played a crucial role in the first stage of reforms by helping the introduction of a new welfare system, in the second stage by facilitating the continuation of reforms mediating different interests and needs, and in the third stage of reforms, by calling attention to the necessity to include a social dimension of transformation (Ladó 2003, p. 258). In this context, it can be affirmed that not the absence of corporatism, but rather a form of *state-led corporatism*<sup>39</sup> is the main characteristic of the transition toward a market economy.

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<sup>39</sup> The concept of *state-led corporatism* has been introduced by Vivien Schmidt during a private discussion at the Centre d'études européennes of Sciences Po (Paris) on 7<sup>th</sup> April 2006. Some reference can also be found in Schmidt (2002).

Finally, as far as the financing mechanism is concerned, the general trend occurring in the four Vizégrad countries seems to lead to a rapid devolution of state responsibility in financing the system of social protection through an increase in social insurance contributions and a gradual equalization of employers' and employees' participation rates. With respect to the important issue of how, and how much, taxes are levied on citizens, while during communism the system was distributive in scope, since 1989 taxation tends to produce a diversified impact on individuals. In Slovakia the revenues from taxes, as percentage of GDP, are the lowest (30.6%), followed by Poland (35.8%), Czech Republic (36.2%) and Hungary (39.1%), which is the only country close to the EU15 average (40.6%). Looking at the structure of taxation it is clear to see that social insurance contributions as percentage of total taxation in Hungary are equal to the contribution rates in the EU 15, but substantially higher in Czech Republic, Poland and Slovakia. However, it is also important to consider how direct and indirect taxes are levied on citizens, since this may influence the final amount of money that people have at their disposal (or their purchase power), thus influencing the final redistributive character of the welfare state<sup>40</sup> (Adema and Ladaique 2005). What is interesting to note here is how the structure of taxation in the four Vizégrad countries is for the most part based on social insurance contributions and indirect taxes, while direct taxes remain significantly below the EU15 average, both as percentage of total taxation and as percentage of GDP (see Table 3). This implies that taxation continues to have a dual orientation: an employment-related character due to the payment of social insurance contributions, and a collective character due to the revenues raised by indirect taxes, such as VAT and taxes on products, which tend to be accumulated more independently of individual's own income.

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<sup>40</sup> Direct taxes are taxes levied directly on an individuals' income (such as personal and corporate tax), while indirect taxes are usually levied on products (such as VAT, taxes on products or on productions). Taxes on productions are more difficult to discern, since it is not easy for citizens to quantify their impact immediately.

	<b>Total taxes % of GDP</b>	<b>Indirect taxes % of total taxation</b>	<b>Direct taxes % of total taxation</b>	<b>Social security contributions % of total taxations</b>	<b>Indirect taxes % of GDP</b>	<b>Direct taxes % of GDP</b>	<b>Social security contributions % of GDP</b>
<b>Czech Rep.</b>	<b>36.2</b>	31.4	27.1	41.5	11.4	9.8	15.0
<b>Hungary</b>	<b>39.1</b>	42.4	25.0	32.5	16.6	9.8	12.7
<b>Poland</b>	<b>35.8</b>	42.8	20.1	39.4	15.3	7.2	14.1
<b>Slovakia</b>	<b>30.6</b>	37.6	23.6	40.2	11.5	7.2	12.3
<b>EU15</b>	<b>40.6</b>	34.6	33.1	32.5	13.6	13.7	13.2

Source: Eurostat 2005.

Finally, the four Vizégrad countries spend less than Western Europe in welfare programmes, with public welfare expenditures that remain substantially below the EU 15 average<sup>41</sup>. In 2001, for example, the total public social expenditures were equal to 20.1% of GDP in the Czech Republic and Hungary, 23.0% in Poland and 17.9% in Slovakia, while the EU15 average was equal to 24.0%. Similar considerations apply to old age, health care, family and unemployment benefits, although there are some exceptions, such as the case of the Czech Republic for health care and Hungary for family benefits. Here, what is interesting to note is that despite the existence of raising unemployment, only Poland, comes close to the EU15 average for expenditures on unemployment of 1.2% of GDP (see Table 4).

	<b>Total</b>	<b>Old Age</b>	<b>Health care</b>	<b>Family Benefits</b>	<b>Unemployment</b>
<b>Czech Rep.</b>	20.1	6.7	6.7	1.6	0.2
<b>Hungary</b>	20.1	8.0	5.1	2.5	0.4
<b>Poland</b>	23.0	8.5	4.4	0.9	1.0
<b>Slovakia</b>	17.9	6.7	5.0	1.5	0.5
<b>EU15</b>	24.0	8.8	6.1	2.2	1.2

Source: OECD Social Security Expenditure Database 2004

<sup>41</sup> Please note that very little, information is available in the *OECD Social Expenditure Database 2004* on private welfare expenditures in Central and Eastern Europe. The analysis here thus concerns only public social expenditures, that is, the expenditures provided by public authorities, with the exclusion of compulsory and voluntary private programmes. Private provisions corresponds, at the moment, only to a small part of total social expenditures, usually not above one percentage point of GDP.

## Conclusion

If one looks at the reform trajectories prior to the fall of the Berlin Wall, similarities with the reform trajectories in other Bismarckian countries (such as France) can be found. These similarities can partly be explained by similar external economic shocks that the countries of Central and Eastern Europe were facing (such as the oil crisis of the 1970s), but also by the existence of similar Bismarck-oriented welfare institutions. Expansion of welfare provisions during the 1970s and the early 1980s in CEECs was largely associated to an increase in external debt and in social insurance contributions. Modifications in social policy remained under the dominant communist logic, but Bismarckian features, already present, became more preponderant (*the golden age*). After a brief period, where welfare institutions were called to amortize the costs of economic transition (*the era of forced expansion*), attempts of welfare retrenchment characterized the policy trends in these countries in the 1990s. In comparison with other Western democracies, the political discourse in these years focused on the necessity to ensure system and financial stability. In the Central and Eastern European case, this was also linked to the future consolidation of democratic institutions (*the era of retrenchment's attempts*). More recently, alteration and amendments in the national legislation are taking place in almost all welfare state sectors, involving the reduction, but also, in some cases, the expansion of the level of benefits (first order changes), as well as the introduction of new calculation rules, new kinds of entitlements and benefits (second order changes). These changes tend to go beyond simple "retrenchment" policies, since they aim to recalibrate the system to the new emerging social problems, which are now different for the early days of post-communist transition (*the era beyond retrenchment*).

Central and Eastern European welfare states can in fact be seen as a laboratory where new social policy instruments (such as the three-pillar scheme or the Minimum Subsistence Level) are tested and, if problems arise, these instruments are immediately modified and adjusted to the new needs. The best examples of policy learning in the region are the continuous adjustments in the pension and health care sector<sup>42</sup>. Here, first

<sup>42</sup> The Czech pension insurance Act No. 155/1995 has been amended several times since its establishment. The latest revision, Act No. 264/2002, entered into force in July 2002 concerns the increase of old age benefits based on the increase of consumption prices and real salary index. In Hungary, the latest amendment of the pension legislation, Law 54/2004 amending Law 82/1997 on private pension and private pension funds, gives certain persons the possibility to change from the private pension scheme to the social security pension scheme. In Poland, the latest amendment of the pension legislation, Act of 30 April 2004 on early retirement (Text No. 1552), provides the new rules for eligibility criteria as well as the monthly amount of benefits. In Slovakia, the Act No. 43/2004 on pension saving schemes, which amends Act No. 461/2003 on social insurance, now forbids any discrimination (direct or indirect) concerning pension saving schemes (e.g. sex, marital or civil status, race, colour, language, age, etc.). Same considerations apply to the health insurance legislation, which, in all four Vizégrad countries, has primarily involved a redefinition of responsibilities previously given to local authority, as well as an increase in coverage for non-protected groups. For a complete

and second order changes primarily involve the redefinition of the level of benefits, rules and principles, according to more socially oriented goals than those proposed by the first neo-liberal governments. Protection against unemployment, social assistance and family benefits are not an exception to this trend.

Thus, as argued in previous work (Cerami 2005), Central and Eastern European countries seem to develop around a new welfare logic, which has path-dependent and innovative components. These have been identified in: (a) the re-enforcement of Bismarckian-oriented policies as heritage of the Austro-Hungarian empire (path-dependent); (b) the maintenance of egalitarian and universal aspirations as fostered during the communist period (path-dependent); and (c) the introduction of market-friendly welfare provisions (innovative). If analyzed in their global context, the abovementioned characteristics are evidence for a significant degree of cohesion among these welfare states in transition and may allow for the emergence of a new and unique model of solidarity, in which different *worlds of welfare* coexist and are recombined together. To use a definition recently provided by Lamping and Rüb (2004, 2005) for Germany, the welfare regime in Central and Eastern Europe can, therefore, be described in terms of a "recombinant welfare state"<sup>43</sup>, where Bismarck features remain preponderant. In fact, as Kathleen Thelen (2004, p.293) puts it: "formal institutions do not survive long stretches of time by standing still". To conclude, as highlighted by other papers (see, for instance, France by Bruno Palier 2000, 2005, Spain by Ana Guillén 2005, Germany by Karl Hinrichs 2005), Bismarckian welfare states are not as "frozen" as they seem. Rather, they are *defrosting* their most *immovable objects* (Pierson 1998): a process that is leading to a hybridization of the system.

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and updated list of all amendments in the social security legislation, please see the ILO-NATLEX database.

<sup>43</sup> For Lamping and Rüb (2004, 2005), the German welfare state is in transition from the classical Bismarckian type to an "uncertain something else" that the authors cautiously call a "conservative universalism". Please note that the term *recombinant property* has first been used by Stark (1996) and Stark and Bruszt (1998) to describe the evolution of Central and Eastern European markets.

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Table A1. Reform Trajectories

Types of change	Context	Diagnosis	Content of the policy	Politics of the reforms	Consequences
The Golden Age	<ul style="list-style-type: none"> <li>- Economic downturn (mid 1970's onwards),</li> <li>- social budget deficits</li> </ul>	Social benefits can help the system and (un)democratic stability	<ul style="list-style-type: none"> <li>* Preservation of full employment</li> <li>* raise in social contribution</li> <li>* change in the generosity of the benefits (upwards)</li> <li>* Additional financing necessary raised through external debt</li> </ul>	<ul style="list-style-type: none"> <li>* Raise in social contribution</li> <li>* Unwillingness to cut social benefits</li> <li>* Additional financing necessary raised through external debt</li> </ul>	<ul style="list-style-type: none"> <li>* Continuous welfare expansion beyond the possibility of the central planned economy</li> <li>* Increasing inefficiencies of such policies (impossibility to cope with Western achievements in living standards)</li> <li>* Re-enforcement of Bismarck features as existing before communism</li> </ul>
Forced expansion (before retrenchment's attempts)  NOTE: Temporary and due to exceptional circumstances	<ul style="list-style-type: none"> <li>-Economic collapse following the dissolution of communism</li> <li>- Introduction of market economy</li> <li>- Preparation to a new economic mechanism</li> <li>- Massive socio, political, economic and demographic changes</li> </ul>	The democratic transition has to be rescued, and consolidated	<ul style="list-style-type: none"> <li>* increase in the contributions to social insurance benefits</li> <li>* Introduction of generous early retirement, protection against unemployment and establishment of basic safety net</li> <li>* Reinforcement of Bismarck features</li> </ul>	<ul style="list-style-type: none"> <li>* Negotiated, but based on TINA (There Is No Alternative)</li> <li>* The state takes some responsibilities for the collapse of communism, while at the same time promoting differentiation in risk management</li> </ul>	<ul style="list-style-type: none"> <li>* From social to more individual insurance</li> <li>* Anomalies of the new system covered under state responsibility</li> </ul>
Retrenchment's attempts	<ul style="list-style-type: none"> <li>- Severe economic deterioration</li> <li>- End of what remained of Keynesianism</li> <li>-Global and European orientation/ coordination of economic and social policies</li> </ul>	<ul style="list-style-type: none"> <li>* Welfare systems are seen as partly the cause of the crisis: excessive state involvement reinforce social exclusion; income maintenance is disincentive to work;</li> <li>state involvement damages competitiveness and creates unemployment; state management rules hinder reform capacities</li> </ul>	<ul style="list-style-type: none"> <li>* increasing importance of targeted and market-based benefits</li> <li>* expansion of private provisions</li> <li>* new mode of management (private)</li> </ul>	* Negotiated, but STRONGLY based on TINA (There Is No Alternative)	Weakening of state responsibility, while increasing social insurances mechanisms and actors
Beyond Retrenchment	<ul style="list-style-type: none"> <li>- EU immediate pre-accession</li> <li>- EU Enlargement</li> </ul>	<ul style="list-style-type: none"> <li>Welfare systems need a profound adaptation to the new EU based socio-economic context</li> <li>- Recombinant implementation of EU, OECD, World Bank and IMF ideas in the light of the EU Enlargement</li> </ul>	<ul style="list-style-type: none"> <li>Reconsideration of neo-liberal approach (private pillars in pension, and health insurance are recalibrated)</li> <li>* Activation of unemployed</li> <li>* Competition in health</li> <li>* Emphasis on social inclusion due to Lisbon European Council</li> </ul>	* Negotiated, but based on a new, more socially-aware approach	<ul style="list-style-type: none"> <li>* Recalibration of previous reforms</li> <li>* hybridization of the system</li> </ul>