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TO THE E.U. SOCIAL PROTECTION COMMITTEE

ANNEX TO THE REPORT ON THE SPANISH NATIONAL STRATEGY FOR THE FUTURE OF THE PENSION SYSTEM

Applying the open method of co-ordination in the area of pensions

Madrid, 12th September, 2002

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I. INTRODUCTION

The basic principles of the Spanish system of social welfare are set out in article 41 of the Constitution of 1978, which reads: “The public authorities shall maintain a public social security system for all citizens to guarantee them sufficient care and social benefits in situations of need, especially in the case of unemployment. Complementary care and benefits shall be optional.”

The result of putting this constitutional mandate into practice has been a social welfare model which is based on the following structure of protection:

The first pillar of public social protection in Spain consists of two levels:

- A basic, universal and means-tested level of non-contributory benefits, financed by taxation. It includes non-contributory financial benefits, health care, family benefits and social services.

- A second occupational and contributory level which is obligatory for all employees or self-employed people. Its protection consists of income substituting wages in cases of retirement, permanent or temporary disability, maternity, risk during pregnancy and death and survivors coverage. This level is basically financed by social security contributions made by employers and workers.

These two levels make up the first pillar of the social security system. They do not cover certain public sector groups such as civil servants working for central government or the justice system or people working for the armed forces. The social protection offered to these groups is organized and managed by special institutions and regulations.

Complementary and private protection is fundamentally based on three kinds of pension plans: occupational pension plans, which form the **second pillar of protection**; and private and group plans which form the **third pillar of protection**. This protection is voluntary and complementary to that offered in the first pillar. The payments made into the plans are capitalized in favour of the beneficiaries, and managed privately. The benefits can be drawn in the form of regular or lump-sum payments covering retirement, invalidity, death and survivor’s coverage, etc.

II. THE SPANISH SOCIAL SECURITY SYSTEM

The present system is regulated by the Royal Legislative Decree 1/1994, which passed into law the Reworked Text of the General Law on Social Security. It sets out the principles on which the system is run: specifying that contributions into the system are obligatory;

setting out the way these are collected; the risks covered; the protection offered; the economic structure of the system, etc.

The public system has developed into the two levels of the first pillar of protection: the basic and the contributory. The basic level is universal, and is financed by taxation. It includes health care benefits, non-contributory pensions, family protection and social services. In general, people receiving these benefits have to prove their lack of sufficient means.

The contributory level protects people who are working in Spain. It is financed mainly by social security contributions and offers financial benefits substituting wages in situations of need resulting from private or working life. Those covered by this level also have the right to health care and social services.

The following analysis of both levels of the social security system concentrates on its four main elements: field of application, protection, economic and financial structure and institutional structure.

The field of application is defined as the population group covered by the system. It thus refers to the affiliated workers, all the pensioners and the beneficiaries of each of the different schemes within the system.

Protection consists of benefits, both financial and in kind, which are offered to those within the field of action when one of the eventualities covered occurs, whether it is in ordinary life or work-related.

Although the extent of protection is essentially the same for both ordinary life and work-related situations, in the latter case there are certain minor differences. These include the fact that a minimum period of contributions is not required in order to receive benefits; that there is a higher base rate for calculating the amount of benefits; and that there is specific compensation for permanent non-disabling injuries and death.

Contributory pensions are the most important part of protective action, both in terms of the number of beneficiaries and the amount of their pensions, and because of the fact that they represent the only income, and thus the only means of support, for the people receiving them. These pensions are financial benefits paid regularly either for life or until a certain age is reached.

The amount of the contributory pension is determined by the following three factors:

- The *initial pension*, which itself depends on two factors: the calculation base obtained as an average of the contributions paid in by the worker; and the percentage coefficient applied to this base according to the type of pension.

- The annual *increment* paid to maintain purchasing power. The reference used for the increment is the increase in the Consumer Price Index.

- The *minimum top-up* which guarantees a minimum level of income for people with low pensions.

These three factors constitute the gross value of a pension. To obtain the net value, the only deduction applicable to pensions is income tax, and this is applied in the normal way, except in the case of permanent total invalidity pensions, which are tax-free.

The economic and financial structure of the social security system is designed to guarantee a balance between expenditure and revenues. There are basically two sources of revenues: social security contributions, which are used for payment of contributory benefits; and state taxation, which guarantees payments at the non-contributory level.

Making up the institutional structure of the system are bodies managing the various benefits; the General Social Security Treasury; the mutual industrial accident and illness societies (employers' associations which collaborate in the management of cases of industrial accidents and illness); and companies chosen on an individual basis which can collaborate in the management of certain benefits related to their own workforces.

III. LEVEL I: PUBLIC AND BASIC: NON-CONTRIBUTORY BENEFITS

III. 1. Field of application

The field of application for this level is based on the principles of universality, means-testing and finance from the central government budget. The benefits and people who can receive them are as follows:

- Non-contributory pensions: the conditions for receipt of these are that the beneficiaries should prove a minimum period of legal residence in Spain, that they should have financial resources below a minimum level established annually, and that they should be ineligible to receive contributory benefits.

- Child benefits: these are for Spanish people and legally resident foreigners who have dependent children. The child also has to be legally resident in Spain or, though living outside Spain, must have the right to reside in Spain with the person receiving the benefit.

- Health care: this covers people who receive non-contributory benefits and people included in the contributory part of the social security system, as well as all other people registered as living in Spain who are not part of the contributory social security system, as long as their annual income is below the minimum wage.

- Social services: the field of application for these is the same as for child benefits.

III. 2. Protection

Protection at this level includes a series of financial benefits and benefits in kind. The former are non-contributory pensions, unemployment benefit and child benefit; the latter, health care and social services.

III.2.1 *Non-contributory pensions*

These are fixed-amount financial benefits for invalidity or retirement. They receive an annual increment through the central government budget.

The non-contributory retirement pension is given to people when they reach 65 years of age, have no financial means of support and do not have the right to take advantage of the contributory system because they have not paid enough contributions, or any at all, into the system. The monthly pension of this kind in 2002 is 258.68 euros, paid 14 times a year.

Non-contributory disability pensions are paid to people aged under 65 who have a level of physical or mental disability of at least 65%, who do not have adequate financial means of support and who are not eligible under the occupational or contributory system. The amount is the same as that of the retirement pension.

III.2.2. *Child benefits*

Child benefits can be in the form of regular payments or as a lump sum:

III.2.2.1 *Regular payments*

The conditions for receiving this payment are: having dependent children of under 18 years of age and an annual income below an amount determined annually in the central government budget; or having older dependent children who are affected by a disability of 65% more, as long as they do not have the right to contribution-based benefits for this reason.

The amount depends the child’s age and degree of disability. The monthly amounts in 2002 are as follows (in euros):

Child benefiting	Monthly amount
Child <18 not disabled	24.26
Child <18 disability >33%	48.48
Child >18 disability >65%	251.00
Child >18 disability >75%	376.50

III.2.2.2. *Lump-sum financial benefits*

A benefit for the birth of a third or successive child is paid to families whose income is below a certain level, which is determined annually. The benefit is a lump-sum payment which in 2002 is 450.75 euros.

The multiple-birth benefit is given to all families in which the mother gives birth to two or more children. The amounts paid depend on the number of children born, and for 2002 they are as follows:

Number of children born	Amount (in euros)
2	1,768.8
3	3,537.6
4 or more	5,306.4

III.2.3 *Health care*

This includes primary health care, specialist care, hospitalisation and medicines, as well as other complementary benefits.

III.2.4 *Social services*

These aim to complete the protection of pensioners. They offer facilities which help improve the level of social welfare and increase the standard of living, and also deal with situations of need among the elderly or disabled.

The measures included under social services are here broken down according to the target groups:

III.2.4.1 *Care for the elderly*

Situations of need for the elderly are met in the following ways:

- *Residential homes for the elderly.* These are homes for people aged over 60 which offer comprehensive and round-the-clock assistance. There are also special centres for people who are unable to care for themselves.

- *Day centres for the elderly*. For people aged over 60, or under 60 in the case of a younger spouse, these act as social and information centres, as well as offering any necessary health care or attention required.

- *Telephone home help*. This service is offered to elderly or disabled people via the telephone. They can alert carers at a professionally-staffed centre 24 hours a day by pressing a special key on their phones.

- *Health spas*. The scheme facilitates visits to spas by pensioners within the social security system, as long as they have been prescribed such a visit by their doctor.

- *Social tourism*. This programme offers holidays, mainly in coastal areas, for people aged over 65.

III.2.4.2 *Care for the disabled*

The following kinds of centres are specially run for this group:

- *Care centres for the disabled*: These are centres with the facilities to offer special care programmes for the disabled. They include centres for the rehabilitation of the physically disabled and care centres for the social and occupational integration of the physically and mentally disabled. In addition, there are occupational training centres.

- *National Centre for Personal Autonomy and Technical Assistance:* This centre is specifically aimed at improving access to a wide range of services and developing technology which improves the quality of life, in particular for the disabled or elderly. Its target areas of activity are making buildings, transport and urban development more accessible, increasing access to computers, adapting jobs, making houses more ergonomic and comfortable for the elderly and disabled, etc.

III.2.4.3 *Assistance for immigrants*

- *Refugee residential centres (CAR):* These public centres are for people who seek asylum in Spain and are granted the status of refugees or displaced persons, but do not have the financial means to look after themselves and their families. The centres offer accommodation, board and primary and emergency socialisation support, as well as other social services which help facilitate social integration. The maximum length of stay in these centres is six months.

- *Temporary immigrant residential centres (CETI)*: These are designed as a primary reception service for immigrants. They cater for basic needs such as accommodation, board and health care, as well as offering the necessary social and employment tools for integration into Spanish society.

III.3. Economic and financial structure

The resources for expenditure at the public and basic level come from the central government budget. This system, which is the result of a gradual process culminating in 2000, is based on the Recommendation 1 of the Toledo Pact and the provisions of Law 24/1997 governing the consolidation and rationalisation of the social security system. In addition, a new system of regional finances has been implemented as a result of an agreement between central government and the autonomous regions. This establishes the principle of fiscal co-responsibility, under which the autonomous regions pay for the cost of health care and social services, in return for a transfer of tax revenues.

III. 4. Institutional structure

As a result of the agreement mentioned in the previous paragraph, the benefits are managed by the corresponding social and health services of each autonomous region.

IV. LEVEL II: PUBLIC AND CONTRIBUTORY

IV.1. Field of application

People legally resident in Spain, whatever their sex, marital status or job/occupation, are covered at the contributory level of the social security system, as long as they work within the country. All workers within the social security system as well as their families are included in one of the social security schemes outlined below:

- *General scheme:* This is the main scheme, and includes employees in most sectors aged over 16, whatever their form of contract, job category or salary.

- *Special schemes*: These include workers in sectors with special characteristics, whether because of conditions of their work, their form of employment, or their wages. They are: the Special Agricultural Scheme, the Special Scheme for Workers at Sea, The Special Scheme for Self-Employed Workers, the Special Scheme for Domestic Workers and the Special Coal Mining Scheme.

The scheme to which the worker belongs determines the kind of risks and situations which are protected, the contributions paid as a percentage of wages and the amount of benefit received. However, the most recent changes made to the system have tended to reduce the differences between the schemes. The 9 April, 2001 agreement between the government and the social partners included the decision to transform the system gradually into one made up of two basic schemes: one for employees and one for self-employed workers. The level of protection within the schemes will be evened out, as will the level of contributions.

For reasons of space, the analysis in this section will be restricted to the majority group, which is that of employees in the general scheme.

IV.2. Protection

All workers included in the occupational level of the social security system who comply with the relevant requirements have the right to the financial benefits described here. In general, all contributory pensions are subject to annual increments at the beginning of each year according to the forecast increase in the Consumer Price Index (IPC) for the year. If the actual IPC at the end of the year is greater than that forecast, the pensions are increased correspondingly. At the same time, all pensions have a guaranteed minimum level, according to the type of pension, the age of the pensioner, and his or her family situation.

IV.2.1. Pensions

a) Retirement

This is a lifelong benefit paid to a worker in any of the social security schemes, when he or she stops working partially or entirely because of age and has paid contributions for the requisite number of years.

Workers who are in the social security system, or who comply with certain criteria giving them assimilated status, and who meet the following requirements can receive the benefits paid:

- If they have complied with the *contribution period* of at least 15 years, of which two have to be during the 15 years prior to retirement.

- If they are at retirement age, which is 65. However, this age limit may be reduced for workers in the following circumstances:

  - If they began to pay contributions into the social security system after 1 January, 1967, people aged over 61 may receive an early retirement pension if they have paid into the system for at least 30 years, were laid off against their will and have been registered as unemployed for the previous 6 months. In this case, the amount of pension is reduced by the percentages given below for each year remaining before the age of 65.

Years of contributions	Percentage of reduction per year
30 years	8%
31 to 34 years	7,5%
35 to 37 years	7%
38 to 39 years	6,5%
40 years or more	6%

  - Workers who paid contributions before 1 January, 1967 may take voluntary early retirement from the age of 60 with a reduction in pension of 8% for each year remaining until the age of 65. However, if the worker has been laid off against his or her will, and has made contributions into the system for more than 30 years, and has been registered as unemployed for at least 6 months, the reduction of pension for each year will be according to the table above.

Since 1 January 2002, the base rate for calculating retirement pension has been the average of the contribution bases for the 15 years immediately before retirement. The amount of pension is calculated by applying a percentage to the base rate according to the total years of contributions. The percentages are as follows:

Years of contributions	Percentage applicable
15	50%
16 to 25	3% extra per year
26 to 35	2% extra per year
35	100%

If the worker retires aged over 65, with more than 35 years of contributions, the percentage applicable to the base rate is 100% plus 2% more for each complete extra year worked after the 65th birthday, or after the date on which 35 years of contributions were made, if this is later.

Thus the amount of the pension is the result of applying the percentages outlined above, which depend on the years of contributions, to the base rate. If the pensioner is under 65 years of age, the corresponding reduction is applied, as explained. The pension calculated is paid in 14 payments a year.

Since 1 January, 2002, workers who have made contributions for at least 35 years and who retire aged over 65, have their pensions calculated by applying a percentage of 100% to their base rate, plus 2% for every additional complete year which they have worked after their 65th birthday. A full pension cannot be paid if the pensioner is working, though the reform introduced 1 January, 2002 allows retired people to combine a pension with part-time work. Under this “flexible retirement” scheme, the proportion of the pension received will be equal to the proportion of the full-time working day for the job which is not worked by the pensioner.

Another form of retirement is that called “part-time”. This can be taken by workers of 60 years or older, whose working day and salary are reduced by a figure of between 25% and 85%. The condition is that, at least until the pensioner is 65, the company must recruit an unemployed person for working hours which are at least equal to the reduction taken by the part-time pensioner. In this case, wages are compatible with a reduced pension, until the pensioner retires completely.

b) Permanent incapacity

This situation applies to workers whose capacity to work is reduced or completely lost, either temporarily or permanently, as assessed by the services of the National Institute for Social Security. The incapacity may be the result of events in ordinary life or at work. There are different levels of incapacity, according to the degree of reduction or complete loss of capacity to carry out the former job:

- *Permanent partial incapacity for the normal job*: This is an incapacity which results in a reduction of 33% or more in the worker's ability to carry out his or her job, although it does not prevent the execution of the basic tasks required by the job.

- *Permanent total incapacity for the normal job*: This prevents the worker from carrying out his or her job, though he or she may still be able to work in other jobs.

- *Permanent absolute incapacity for all work*: This is paid if the worker cannot work in any kind of job.

- *Major disability*: This means that the worker needs the help of others to deal with the most essential aspects of daily life.

Those eligible for this benefit are workers who have been registered as incapacitated and have paid into the system for a certain time, which depends on the age at the time of disablement. In the case of workers over the age of 20 it is five years.

The amount of the benefit depends on the degree of disability registered:

- The benefit for permanent partial incapacity is a lump sum equivalent to 24 monthly payments of the calculation base used to determine the benefit for temporary incapacity.

- The benefit for permanent total incapacity is a pension equivalent to 55% of the calculation base, with this amount being increased by 20% for people over the age of 55 who have problems finding a job.

- The benefit for permanent absolute incapacity is 100% of the calculation base.

- The pension for major disability is 150% of the calculation base, with the extra 50% being for the person who has to care for the disabled person.

In general, the calculation base of the pension is the weighted average of the calculation bases of the previous 8 years. In the case of industrial accidents, the base corresponds to the wage on the day of the accident.

When a decision is made to pay a permanent incapacity benefit, in whatever form, a future date is also fixed for a possible revision of the type of benefit according to any improvement or worsening of the condition of the disabled person.

When people receiving pensions for permanent incapacity reach 65 years of age the pensions become "retirement pensions". The new name does not mean any change in the amount of money paid.

c) Death and survivor's coverage

These are benefits resulting from the death of a worker, regardless of the cause. The benefits in this case are: widow's pension, orphan's pension and relatives' benefits. If the death is the result of an industrial accident or illness, damages are paid in addition to the corresponding pension.

c. 1) *Widow's pension*

The beneficiaries of a widow's pension are the surviving spouse, or former spouse if separated, divorced or with the marriage legally annulled.

In general, this pension depends on the person who dies being in the social security system or complying with certain criteria giving him or her assimilated status at the time of death, and having paid contributions for at least 500 days in the 5 years immediately prior to death, if the deceased was of active age. If the deceased was a pensioner, no minimum period of contributions is necessary.

Until 31 December, 2001, the size of the pension was equivalent to 45% of the average base rate of contributions for the previous two years. As of 1 January, 2002 it is 46% of the calculation base for the period. The agreement of 9 April for the improvement and development of the system of social protection stipulates that this figure should be gradually increased to 52%. If the pension represents the main or only source of income and the pensioner has dependent family members, the percentage applied to the calculation base 70%.

c.2) *Orphan's pension*

The beneficiaries of this pension are children of the deceased under 18 years of age, or older if they are disabled. If the annual income of the beneficiary is 75% or less of the minimum wage, he or she may receive the benefit until the age of 22, or 24 if both parents are deceased.

Eligibility for the pension, in terms of being in the social security system and having paid the necessary contributions, is the same as for the widow's pension.

The amount of the pension is 20% of the average calculation base of contributions for the previous two years. In the case of orphans with both parents deceased, the 20% is increased by the 46% corresponding to the widow's pension, and this amount is divided equally between each orphan in the family. If there is more than one beneficiary, the sum of the pensions may not be greater than 100% of the calculation base of the combined pensions.

c.3) *Relatives' benefits*

c.3.1) *Pension for relatives*

The beneficiaries of this pension are family members up to the second degree of kinship (spouse, parents, children, brothers and sisters, grandparents or grandchildren) who lived with and were financially dependent on the deceased for at least two years before his or her death. The pension is dependent on their not having the right to any other state pension and having no adequate means of support.

The amount of the pension is calculated by applying a factor of 20% to the calculation base applicable for widow's and orphan's pensions. If the deceased does not leave a surviving spouse or children, the 20% is increased by the 46% corresponding to the widow's pension.

c.3.2) *Relatives' allowance*

Those receiving this benefit are children and brothers or sisters who are single or widowed and over the age of 22 when the death occurs, and who satisfy eligibility requirements outlined above for the pension for family members.

The amount is paid for 12 months, with 2 extra payments (14 in all), and is calculated by using a factor of 20% on the calculation base for the widow's pension.

IV.2.2 Other financial benefits

The benefit for Temporary Incapacity is paid to workers who are temporarily incapacitated and unable to work as a result of a normal or work-related illness or accident. The benefit is for up to 12 months, but can be extended for six-monthly periods up to a maximum of 30 months. The amount depends on the calculation base for contributions for the month before the period of incapacity begins. In the case of illness or accidents which are not work-related, 60% is applied to the calculation base between the fourth and twentieth day, and 75% from the twenty-first day on. In the case of work-related illness or accident, the percentage is 75% from the day after the period of incapacity begins.

The benefit for Risk During Pregnancy is paid when the work carried out can injure the health of the mother or the unborn baby and the company cannot transfer the worker to another comparable job, for justifiable technical reasons. The amount is calculated by applying 75% to the calculation base used for temporary incapacity.

Maternity benefit covers the leave taken for maternity, adoption or fostering, including the period before adoption, as long as the children are under 6 years of age (or over in the case of disabled children or those with social or family problems). The amount is equivalent to 100% of the calculation base of the month before the leave is taken. The leave available is 16 complete weeks, which in the case of multiple childbirth, adoption or fostering may be increased by two weeks extra for each child after the first.

Other benefits in the system are damages for permanent non-incapacitating injuries and special damages in the case of death by industrial accident or illness.

IV. 3 Economic and financial structure

The contributory level of the social security system is financed by distribution. This method is applied in all cases and situations included in each of the schemes. The only exception, in certain cases, is payment for industrial accidents, which uses a capital finance system of coverage.

IV.3.1 *Sources of finance*

The General Law on Social Security stipulates that, under the general pensions scheme, both workers and their employers have to make contributions, except in the case of risks of industrial accidents and illnesses, for which the contributions are paid exclusively by the employer. The employer is responsible for ensuring that contributions are made by paying in both his or her own contributions and those of the company's employees.

The amount of contributions is determined by the calculation base and the percentage of contribution, both of which are set out in the central government budget every year. The calculation base is the total remuneration received by the worker, within certain maximum and minimum limits established annually by the budget. If the wage is below the minimum limit, the contribution is calculated according to the minimum calculation base; if it is above the maximum, it is calculated according to the maximum. The amount of contributions paid is calculated by multiplying this figure by a coefficient which varies according to circumstances. Under the general scheme, the single overall rate which finances contributory benefits is 28.3%, with 23.6% paid by the employer and the remaining 4.7% by the employee.

Under the special schemes, the calculation bases and the coefficients applicable are different for each scheme. For example, under the special scheme for self-employed workers, there is a minimum and maximum calculation base. The contributors can choose, within certain limits, the base within these two amounts. The percentage rate for this scheme is 28.3%, or 26.5% if the self-employed contributors decide not to pay for voluntary insurance against temporary incapacity.

IV. 4 Institutional structure

The social security system is structured around a series of managing bodies, joint services and collaborating bodies. The benefits are managed publicly through the following bodies:

- The National institute for Social Security (INSS): The INSS awards and controls all contributory benefits, except unemployment benefit and the benefits which the Social Marine Institute (ISM) manages under the special scheme for workers at sea. The INSS also manages family child benefits and awards the right to health care.

- The Social Marine Institute (ISM): This is a specific integrated body which regulates and manages protection for workers at sea.

The General Treasury is a joint service which carries out tasks affecting the other bodies within the social security system. It oversees the economic resources available and carries out the financial management of the system, applying the principles of solidarity and centralised incomes and payments. It registers workers, collects contributions, organizes payments and distributes available funds to prevent shortfalls. This joint service is also responsible for the Social Security Computer Operations Centre.

The management of the social security system, which in general is carried out by the managing bodies, can also be the responsibility of the mutual industrial accident and illness societies or of employers. The mutual societies are associations of employers, recognized by the Ministry of Labour and Social Affairs, which are set up with the main objective of collaborating in the management of cases of industrial accidents and illness, prevention of risk at work, rehabilitation of workers and assisting in the management of benefits paid for temporary non-work related incapacity. Individual companies may also be allowed to collaborate in the management of certain benefits paid to their own workers.

A commitment has been reached to change this management structure through the creation of the Social Security Agency. The agency will improve efficiency by integrating the registration of new contributors, collection of contributions and management of benefits.

V. LEVEL III: PRIVATE AND COMPLEMENTARY

The first two levels of public and obligatory social protection, described above constitute the social security system. In addition, there is a third complementary level, the basic components of which are pension funds, life insurance, mutual insurance societies and, for the time being, internal funds. Pension funds are private institutions offering free and voluntary provision for their members, giving participants the right to receive income or capital at retirement, widowhood, orphanhood or disability. Pension funds may be a complement to the obligatory social security system, but in no case are they a substitute. The law establishes the principle of non-discrimination, guaranteeing access to a pension plan for any individual who meets the conditions for joining and entering into the contract for the plan.

From the strictly financial point of view, pension plans are based on financial and actuarial systems of individual capitalization. Regular payments into the system and their interest accumulate until they form sufficient reserves to generate the benefits designed by the plan.

By definition, pension plans are divided into the following schemes:

- The occupational system: These are plans whose sponsor is any body, corporation or company and whose participants are its workers.

- ♦ Group system: These are to plans whose sponsor is any association, trade union, guild or group, and its participants are associates, members or affiliates. These groups have to be defined by some joint characteristic other than the fact that they sponsor a pension plan.

- ♦ Individual system: These are plans whose sponsor or sponsors are one or more financial bodies, and whose participants are any private individuals, except people who work for the sponsor and their family members up to the third degree of kinship (i.e. including uncles, nephews and nieces, great grandparents and great grandchildren).

In the case of occupational pension plans, the commitments must be externalised, i.e. the employer cannot be the guarantor of the coverage of these commitments through the creation of internal funds or similar instruments if they mean that the employer continues to be the title holder of the assets.

The externalisation of pension commitments by companies fulfils a twin objective. Firstly, it protects the interests of the workers and beneficiaries in case of bankruptcy or financial difficulties; secondly, by keeping pension commitments off the balance sheet, companies can free assets and concentrate on their real business activity thus, in the final analysis, increasing competitiveness. In addition, the process means that the management of these assets is carried out by organisations specialising in financial management and investment, representing a lower cost and increasing the capitalisation of the economy by boosting long-term savings.

In terms of taxation, the present system relating to pension plan contributions and benefits postpones the income tax payable by participants to the moment or period in which they receive the benefits, while the contributions to the plans are income tax-deductible up to a certain point. Pension funds themselves, which are theoretically subject to corporation tax, pay no tax.

Finally, we should highlight the positive contribution made at this complementary level by the social partners, the government and the different political parties across the parliamentary spectrum, as reflected in the various agreements signed until now.

VI. CHANGES AND REFORMS IN THE SOCIAL SECURITY SYSTEM

The Spanish social security model has shown a dynamic ability to adapt to changing social and economic circumstances through various reform processes. The aim has been to maintain long-term financial and economic stability, increase protection and strengthen the effects of redistribution and solidarity, and to modernise in line with new conditions and social situations. The main reforms have been based on the following social and political agreements:

- ✓ Economic and social agreement of 1984.

- ✓ The Toledo Pact, passed by parliament in 1995.

- ✓ The 1996 agreement between the government and main trade unions to implement the recommendations of the Toledo Pact.
- ✓ The 1999 agreement on the increase of minimum pensions for 2000.
- ✓ The 2001 agreement to improve and develop the system of social protection.

The legislation which has passed these reform measures into law is the following:

- ✓ Law 26/1985 of urgent measures for the rationalization of the structure and protective action of the social security system.
- ✓ Law 14/1986, the General Health Service Law.
- ✓ Law 8/1987 on pension plans and funds.
- ✓ Law 37/1988, the central government budget for 1989, which modified the structure and operation of the protective aspect of the social security system.
- ✓ Law 26/1990, creating non-contributory benefits in the social security system.
- ✓ Law 24/1997, consolidating and rationalising the social security system.
- ✓ Law 39/1999 on the reconciling of work and family life.
- ✓ Law 35/2002, establishing measures for a system of gradual and flexible retirement.

The reforms have been based on the following basic criteria:

VI.1. Improving protection and strengthening the principle of solidarity and redistribution

The first example of these reforms is Law 26/1985, which introduced the idea of index-linking pensions to the forecast rise in the Consumer Price Index for the year, thus maintaining their purchasing power. Law 24/1997, continued along this line and included a guarantee clause making up the difference if the actual Consumer Price Index for the year is greater than that forecast at the beginning of the year.

In terms of improving protection, Law 24/1997 increased eligibility for pensions by removing the requirement that the beneficiary should be paying into the social security system at the time when he or she becomes eligible for the pension in the case of retirement or disability pensions. Later, the requirement was also removed from widow’s pensions.

The law also established increases in two kinds of pension: a gradual three-year rise in the minimum amount of widow's pensions when the beneficiaries are less than 60 years old and have family responsibilities; and a gradual increase in the age limit for receiving an orphan's pension from 18 to 21 and from 21 to 23 if both parents were deceased.

In 1999 the Pension Agreement Monitoring Commission co-ordinated an agreement between the government and main trade unions. This implemented special increases in 2000 above the rate of inflation for certain minimum pensions and non-contributory pensions.

As a result of the social agreement of 9 April, 2001, January 2002 saw the implementation of the regulations relating to the new age limit for receiving an orphan's pension, which was increased from 21 to 22 and from 23 to 24 in the case of an orphan with both parents deceased. In addition, there was an improvement in the widow's pension, increasing the percentage applicable to the calculation base from 45% to 46%, with the stipulation that this amount will increase in the future to 52%. In certain family situations the percentage is 70%.

Finally, it should be pointed out that the as a result of the Toledo Pact and Law 24/1997, universal health care, social services and family benefits have from the year 2000 been financed entirely from the central government budget.

VI.2. Strengthening the occupational, contributory and proportional character of pensions

The aim of this principle is to ensure that people who have made similar levels of contributions should receive a similar level of benefits. To this end, the following changes have been introduced:

Law 26/1985 of 31 July, rationalising the structure and protective action of the social security system, increased the contribution period necessary to receive a retirement or permanent invalidity pension to 15 years. It also changed the way of arriving at the calculation basis, using 8 years for this purpose, of which the first 6 were incremented according to the Consumer Price Index.

Law 24/1997 of 15 July, consolidating and rationalising the social security system, implemented a gradual increase in the period used to determine the calculation base for retirement pensions. The process was completed on 1 January, 2002, when the period was established as the last 15 years of contributions, instead of the last 8 under the previous law.

In the agreement to improve and develop the system of social protection, signed by the government and social partners in April 2001, the parties committed themselves to take the necessary measures from the year 2003 to ensure the best possible method of calculating benefits is used.

In addition to this, measures have been introduced into the system of contributions to create a better balance between contribution bases and wages. The maximum contribution bases for different categories of employment began to be unified in 1989, and the process was completed this year.

VI.3. Separating the sources of finance for the system of social protection

The aim has been to adapt the sources used to finance the obligations of the social security system to the nature of those obligations, according to whether they are contributory or non-contributory. All non-contributory, and thus universal, benefits are now financed from central government budget, while wholly contributory benefits are fundamentally financed from employers' and workers' contributions.

The first step along this path was Law 37/1988 of 28 December, the government budget for 1989. Breaking with the previous situation, in which there was no link made between sources of finance and specific benefits, from 1989 the government began to set aside funds to the social security in order to finance health care and part of the top-ups for minimum pensions.

This created a model for financing the social security system which takes account of the nature of the benefits: contributory benefits are basically financed by contributions, and the non-contributory benefits by central government funds. Each form of protection is based on the idea of occupational and universal benefits, respectively.

The reform has enabled the extension of the health care system to cover people without means, who were not previously included in the system; and later the establishment of non-contributory benefits in 1990, which were not paid for from social security contributions.

Law 24/1997 of 15 July, consolidating and rationalising the social security system, passed into law the recommendations made in the Toledo Pact, and confirmed the financial division of the social security system, adapting the sources of finance to the nature of the obligations. In accordance with this law, health benefits and services, social services, non-contributory pensions and child benefits are non-contributory. They became totally financed from the central government budget in 2000.

On 9 April, 2001, the government, the confederation of the trade union CCOO, the Spanish Confederation of Employers' Organisations and the Spanish Confederation of Small and Medium-sized Enterprises, signed an agreement, which extends to 2004, as part of the objective of consolidating the social security system. The aim of the agreement is to improve and develop the system of social protection, and it sets a time limit of 12 years for transferring the finance for topping up pensions to a minimum level using central government funds. At present, most of these minimum top-ups are financed from social security resources.

VI.4. Establishing a system of gradual and flexible retirement

As a result of the agreement on 9 April 2001, Law 35/2002 of 12 July modified the present rights relating to retirement pensions.

The main changes introduced were:

- Workers who retire over 65 years of age and with more than 35 years of contributions paid, will receive a pension which is more than 100% of the basic pension. Social security contributions for these workers will be waived while they are employed.

- Access to early retirement has also been extended to workers who began paying contributions after 1 January, 1967, as long as they meet certain requirements relating to length of time worked and the involuntary nature of their stopping working.

- Work has been made compatible with receiving a partial retirement pension after the age of 65.

- Reductions have been introduced in employers' social security contributions for workers aged 60 or more.

VI.5. Reconciling work and family life

The entry of women into the labour market has resulted in one of the most profound social changes in history. The need to facilitate their entry into employment makes it necessary to create a new co-operation and commitment between women and men to allow a more equal sharing of responsibilities in work and private life. Measures have been introduced to stimulate women's entry into the labour market, and Law 39/1999 of 5 November includes the following changes:

- The right to a reduced working day or leave has been extended to workers who have to care for the elderly and diseased. Previously, only those looking after children aged under 3 could take advantage of this facility.

- It has been made easier for men to look after their children from the moment of birth, adoption or fostering by granting the woman the option of choosing whether up to 10 weeks of her 16 weeks of maternity leave will be taken by her or the father. The father may also take paternity leave at the same time as the mother.

- Maternity leave has been extended by two weeks per child in the case of multiple births.

- A new social security benefit has been created, related to risk during pregnancy. The aim is to protect the health of the pregnant working woman when her work may negatively affect her health and/or that of the unborn child. It is applicable when the worker cannot be moved to another comparable job within the company.

- The application of reductions in employers' social security contributions has been extended in the case of substitution contracts offered to unemployed people who substitute self-employed workers on maternity, adoption or fostering leave.

The number of measures of this kind has increased since the 1999 law. In January 2000 new lump-sum family benefits were created for the birth of the third child or a multiple birth, and the conditions giving rise to reductions in social security contributions were once more extended (zero cost for mothers). Additionally, the possibility of maternity leave was also introduced for part-time workers, to make this type of time off more compatible with modern working patterns.

VI.6. Reserve Fund

Law 24/1997 established the creation of the Reserve Fund, thus implementing recommendation number 2 of the Toledo Pact and honouring the commitments expressed in the agreement between the government and the main trade unions in October 1996. The fund will be financed from any surplus in social security contributions after settling the budget. The aim is to reduce the adverse impact of economic cycles on the social security system.

As a result of this legal instrument, and thanks to the surplus which the system began to record in 1999, the first endowment of the fund was in 2000, and since then it has been increased every year as follows:

Amount of the fund

(millions of euros in all three tables)

Year	Initial	Additional	Total
2000	360.6	240.4	601.0
2001	541.0	1,620.0	1,803.0
2002	3,575.0	----	3,575.0
SUM			5,979.0
Interest			41.0
TOTAL			**6,020.0**

This initial total in 2002 is already at the level planned for 2004, being equivalent to 1% GDP, and representing more than one month's pension payments. The total endowment of 3,575 million euros in 2002 was approved by the council of ministers on 5 April and the social security general treasury has been authorized to make the transfer during this year.

Until 31 March, 2002 the situation of the reserve fund was as follows:

Total endowments (2000 + 2001)	2,404
Interest	41
TOTAL	**2,445**

The distribution of the assets was as follows:

Financial assets	1,476
Current account in the Bank of Spain	969
TOTAL	**2,445**

Of the additional amount of 3,575 million euros authorised by the council of ministers in April 2002, 1,052 million is already in the fund's current account and the rest is expected to be paid in between June and September 2002.

With regard to the fund's performance, the current account at the Bank of Spain earned an average interest of 4.78% in 2000, 4.32% in 2001 and 3.29% in the first quarter of 2002. The performance of the portfolio reflected an average weighted interest of 4.44%.

VI. 7. Reforms boosting the labour market

The measures under this heading are contained in Spain's National Employment Action Plans, drawn up within the framework of the European guidelines. The main aims of the guidelines are to help groups which have the greatest difficulties in finding jobs, to make unemployment systems more favourable to jobseeking, and to increase workers' employability.

The main reforms undertaken have been targeted at two groups:

- Groups particularly vulnerable to unemployment.
- Groups with temporary contracts.

Since 1997, reforms have been introduced to increase the recruitment of groups with greatest difficulties in entering the labour market and those which have an excessive rate of temporary employment.

Law 64/1997 began the reform process which has been brought up to date each year since then. The law introduced measures mainly affecting the following groups:

- Unemployed young people.
- Unemployed people over the age of 45.
- Women who are under-represented in certain sectors.
- The long-term unemployed.

The law includes measures to promote the conversion of temporary contracts into indefinite-term ones.

The measures adopted to create incentives for recruitment among these groups have been to offer reductions in employers' social security contributions of between 40% and 60%, according to the type of contract.

Recently, additional measures have been taken through the Royal Decree Law 5/2001 to increase activity specifically for people over the age of 55. The law establishes special reductions in employers' social security contributions for workers aged between 55 and 65 who are given indefinite-term contracts. Under the scheme, the employer will pay only 45% of the employers' contribution in the first year of the contract and 50% during the rest of the time the contract is in force.

Law 35/2002, which establishes gradual and flexible retirement, also offers reductions in employers' social security contributions when the worker is aged between 60 and 64, has an indefinite-term contract and has been with the company for 5 years or more. The reduction is of 50%, and is increased by 10 points every year to a maximum of 100%. The law also includes the waiving of contributions for workers over 65 years of age.

With regard to measures targeting women, the employment promotion programme includes the following:

- Indefinite-term contracts signed with unemployed women of between 16 and 45 years of age will attract a reduction of 25% in the employers' basic social security contributions for 2 years.

- Contracts signed with unemployed women for jobs with a low rate of female employment will be eligible for a reduction in employers' social security contributions of at least 45%, and up to 70% if the woman is over 45 or has been unemployed for 6 months or more.