European Commission

EUROPEAN SOCIAL POLICY NETWORK (ESPN)

Financing social protection

Turkey

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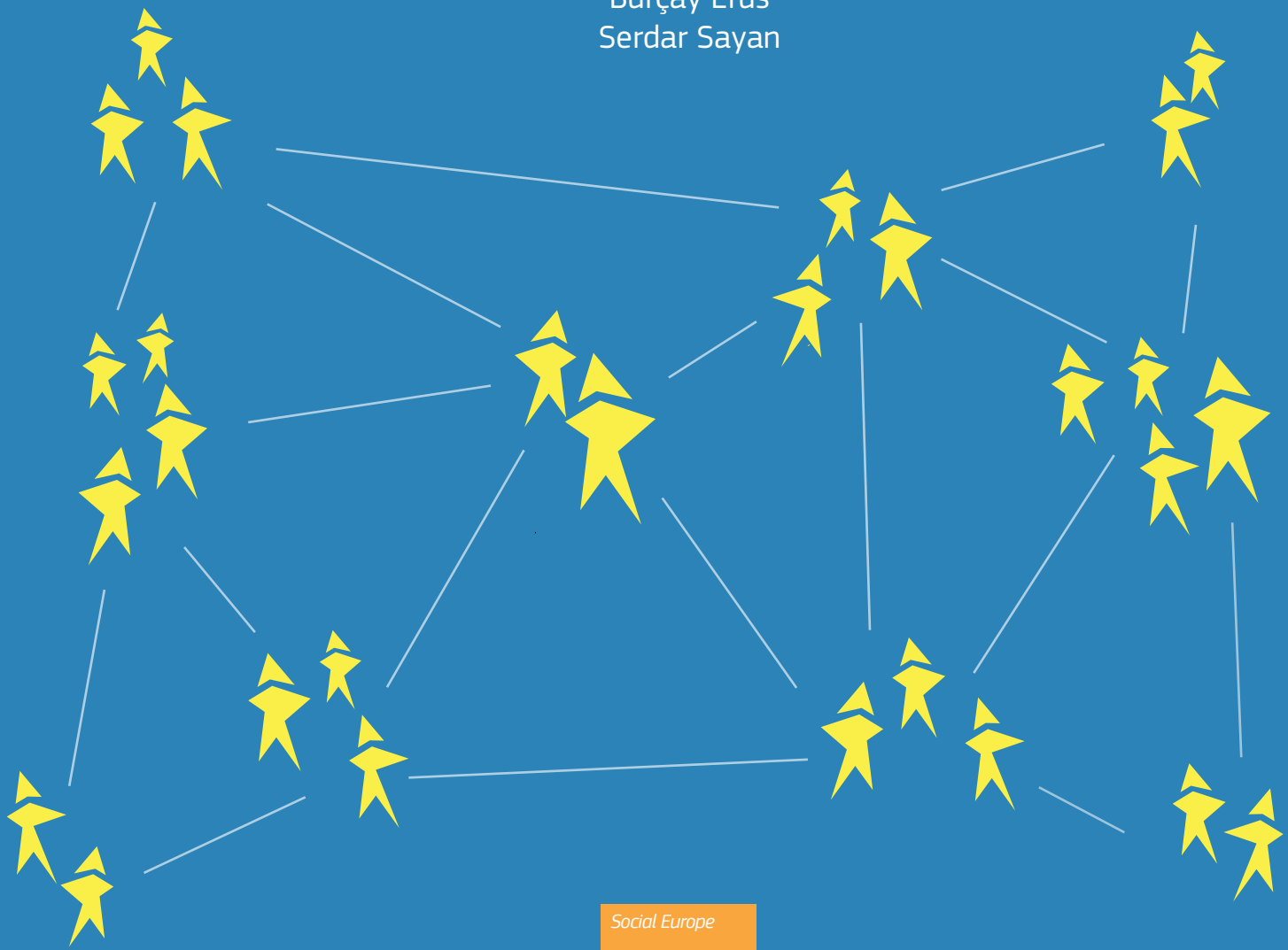

Social Europe

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European Social Policy Network (ESPN)

ESPN Thematic Report on Financing social protection

Turkey

2019

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Directorate-General for Employment, Social Affairs and Inclusion
2019

The European Social Policy Network (ESPN) was established in July 2014 on the initiative of the European Commission to provide high-quality and timely independent information, advice, analysis and expertise on social policy issues in the European Union and neighbouring countries.

The ESPN brings together into a single network the work that used to be carried out by the European Network of Independent Experts on Social Inclusion, the Network for the Analytical Support on the Socio-Economic Impact of Social Protection Reforms (ASISP) and the MISSOC (Mutual Information Systems on Social Protection) secretariat.

The ESPN is managed by the Luxembourg Institute of Socio-Economic Research (LISER) and APPLICA, together with the European Social Observatory (OSE).

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Quoting this report: Adaman, Fikret, Dilek Aslan, Burçay Erus and Serdar Sayan (2019). ESPN Thematic Report on Financing social protection – Turkey, European Social Policy Network (ESPN), Brussels: European Commission.

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Summary

In 2015 social protection expenditure in Turkey made up 12% of GDP.[1] During the decade from 2005 to 2015, expenditure increased in real terms at an average annual rate of 6.7%. Pension payments made up about half of the expenditure in 2015, followed by healthcare expenditure (29.3%), and payments to survivors (11.9%). Social contributions financed 52.3% of the expenditure in 2015, and general government contributions 42%. A large part of government contributions was used to finance the deficit in the retirement system. Health expenditure and unemployment insurance were paid for by premiums, while other social protection expenditure relied on government financing; following reforms made in the pension system, its financial sustainability has been secured.

The deficit in the pension system was largely due to the removal of age limits for retirement from 1992 to 1999 as a result of populist government policies. Although reforms in 1999 reinstated those limits, and reforms in 2005 extended them further, implementation was gradual. As a result, from 2005 to 2015, the number of those on pension benefits almost doubled. An ageing population was also a factor that started to put pressure on the pension system.

During the global economic crisis of 2008, GDP grew by 0.7%; but it then shrank by 4.8% in 2009. The unemployment rate reached 17.5% in 2009 and took its toll on social contribution revenues. As part of its fiscal policy the government reduced some employer contributions for social security in respect of female and youth employment.

Health expenditure is financed by contributions paid for through the universal health insurance system. Reforms have been gradual, with full implementation achieved in 2012. Although increased coverage led to a sharp increase in utilisation and hence expenditure until 2008, the subsequent increase in health expenditure was limited through co-payments and an improved primary care system.

Social assistance expenditure increased dramatically in the period 2005-2015 with new social assistance programmes and improvements in the previous ones. A minimum-income system, however, remained elusive.

Social contributions are not progressive, being levied at the same rate for all income levels up to the cap. Furthermore, general taxation, which funds government contributions, relies heavily on indirect taxes. As such, the financing of social protection adds to significant income inequality.

Structural issues in the political economy cause fundamental problems in financing social protection expenditure, in significant ways. Informality, low labour force participation among women, and persistent unemployment cause heavy costs to be placed on the shoulders of a relatively small pool of contributors to the system. Although policy initiatives have been developed to address these problems, the low level of human capital sits at the root of them.

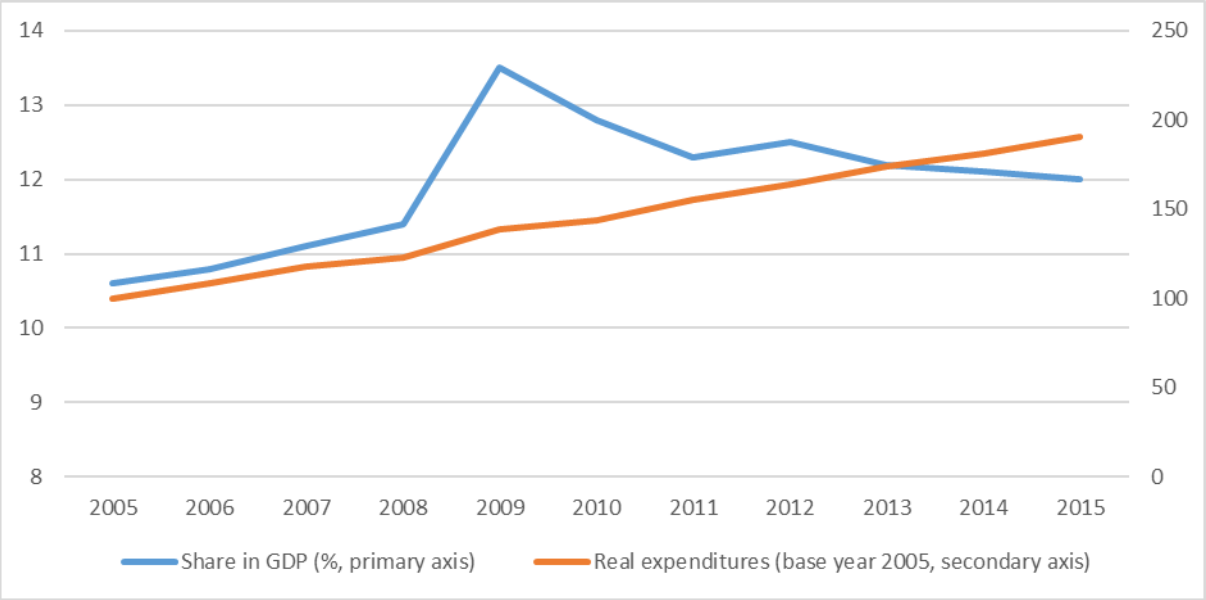
Finally, the recent influx of Syrian refugees has continued to add to social protection expenditure since 2011. Although some contribution has been secured from international organisations, the cost of providing social assistance and healthcare to refugees weighs on the government budget.

[1] All the statistics are from the Annex ESSPROS tables in Spasova and Ward, 2019.

1 Current levels and past changes in financing social protection

Expenditure on social protection in Turkey increased from 10.6% to 12% of GDP between 2005 and 2015. In real terms, as seen in Figure 1, expenditure grew steadily, with a 7.1% average annual increase in 2005-2008, 8.1% in 2008-2010, and 5.8% in 2010-2015. The fluctuations in the ratios to GDP were solely due to changes in the size of GDP, rather than in real expenditure.

Figure 1: Gross expenditure on social protection in Turkey, 2005-2015 (% GDP and in real terms)



Source: Spasova and Ward (2019), Annex ESSPROS (European System of integrated Social PROtection Statistics), tables.

The share of social protection expenditure in GDP in Turkey was very low compared with EU averages of 26% and 28.4% in 2005 and 2015, respectively, and lower than the lowest rate in EU in 2015 (14.6% in Romania). That said, the period under investigation witnessed high GDP growth in Turkey and the level of gross expenditure increased on average by 6.7% annually in real terms, more than four times the annual growth rate for the EU, and higher than all EU members.

Old-age payments made up almost half (48.6%) of social protection expenditure in 2015 (Table 1). Health and sickness expenditure followed with 29.3%. Another 11.9% was spent on survivor benefits. Among the remaining areas, disability accounted for 3.7%, family benefits 3.2%, unemployment 1.9%, and social exclusion 1.4%. Old age and survivor expenditure took significantly higher shares in Turkey than in the EU (for which they were 40.1% and 5.5% respectively), despite its relatively young population. The share of health and sickness expenditure was around the EU average, and the shares of other elements were smaller than in the EU. It should be noted that social expenditure on housing was non-existent in Turkey.

Over the 2005-2015 period, there was a sharp fall in the share of expenditure on health and sickness, from 35.2 to 29.3%. Although spending on old-age and survivor benefits showed a slight increase (from 46.5% to 48.6%, and from 11.8% to 11.9%, respectively), the share of expenditure on disability almost doubled (from 2.1% to 3.7%) and on unemployment it almost tripled (from 0.7% to 1.9%). There were slight increases in the share of family expenditure (from 2.6% to 3.2%) and of social exclusion (1.1% to 1.4%). It should be noted, however, that, as mentioned above, the overall level of social expenditure increased by an annual average rate of 6.7% between 2005 and 2015: even though the share of health expenditure fell, therefore, the absolute level of expenditure on healthcare increased over time.

Table 1: Breakdown of gross expenditure on social protection by function, Turkey, 2005-2015 (%)

	2005	2008	2010	2015
Sickness/Health	35.2	35.5	33.8	29.3
Old age	46.5	47.4	49.0	48.6
Other	18.3	17.1	17.2	22.2
Disability	2.1	2.2	2.9	3.7
Survivors	11.8	10.5	9.7	11.9
Family	2.6	2.6	2.5	3.2
Unemployment	0.7	0.6	1.1	1.9
Housing	0.0	0.0	0.0	0.0
Social exclusion n.e.c.	1.1	1.1	0.9	1.4

Source: Spasova and Ward (2019), Annex ESSPROS tables.
Note: The figure for 'Other' is the sum of the categories listed below it.

The global economic crisis of 2008 had a significant impact on Turkey. GDP grew by only 0.7% in 2008 and shrank by 4.8% in 2009. This was followed by a rapid recovery, with growth rates of 9.2% and 8.8% in 2010 and 2011, respectively. The unemployment rate reached 17.5% in 2009, but fell in the following years, to 12.7% in 2012 (note that due to structural problems the rate has fluctuated around 10% for several decades). While unemployment took its toll on social security premium revenues, as part of its fiscal policy the government also reduced some employer contributions for social security in respect of female and youth employment.

1.1 Pensions

The increase in pension expenditure reflected the significant rise in the number of individuals receiving pensions, from 5.9 million in 2000 to 10.8 million in 2015 according to Social Security Institution (SSI) statistics. In the same period, the population increased from 68 million to 78 million – hence there was an increase in the share of pensioners from 8.7% to 13.9% of the population. The surge in the number of retirees was caused by two challenges faced by Turkey's pay-as-you-go (PAYG) pension system. The first (and the greater of the two) was the remnants of the earlier generous retirement system. The second one was the gradual ageing of the Turkish population.

In 1950, when the retirement system was established, the pensionable age was set at 60. In 1964, that was reduced to 50 for women and 55 for men, and in 1969 it was completely eliminated. The age limit was brought back in 1986, only to be lifted again in 1992 as a result of the government's (extremely populist) decision. The number of contributory days remained as the only criterion for starting to collect pensions. This, in turn, allowed thousands of people to retire in their 40s, causing the worker-to-retiree ratio to fall sharply and pushing pension deficits to unsustainable proportions by the end of the 1990s. In 2016, according to calculations from Turkstat Statistics of Income and Living Conditions, 27.8% of retirees were aged between 46 and 55, and 20.7% between 56 and 65.

Ageing of the population is also a concern. According to Turkstat, the share of those aged 65 and older was 8.2% in 2015, sharply higher than the share of 6.7% in 2005. Life expectancy at birth increased from 74.4 years in 2005 to 78 in 2015.

The pension reform act of 1999 was the first piece of legislation introduced to tackle the rapid growth in pension deficits generated by the (then separate) social security agencies, starting from the early 1990s. The major adjustment brought about by the parametric reform act of 1999 was to reinstate and increase pensionable ages to 58 for women and 60 for men. The act also introduced a cut in replacement rates for everyone retiring after the law came into force. A transition period was allowed for gradual

increases in entitlement ages for those who had already been working in 1999, depending on their seniority at the time. The transition period will end in 2021. By then, some remnants of the previously generous retirement system will still remain.

In 2001, the government passed legislation for the introduction of funded schemes for individuals who want additional pension coverage to complement the benefits provided by the state PAYG scheme. Private insurance companies began to offer individual retirement plans in 2003. In 2013, to further promote (savings for) purchases of complementary pension plans by the working population, the state started to match 25% of all annual contributions (premiums) paid (up to the annual pre-tax total of monthly minimum wages) by individuals to funded pension schemes. Finally, in 2017, all publicly and privately employed wage and salary earners who were younger than 45 were automatically assigned to an individual pension plan, forcing them to start contributing at the minimum rate of 3% of their taxable earnings, unless they requested in writing to opt out within two months of their automatic enrolment in the plan.

Reforms, implemented in 2006 under Law No 5510, were aimed at preparing for the additional financial burden that population ageing would place on the pension system. Reforms stipulated a restructuring of three independent institutions that offered retirement benefits to different groups within the working population (*SSK* – blue-collar workers and white-collar workers employed in the private sector; *Emekli Sandığı* – white-collar workers employed by local and central government; and *Bağ-Kur* – farmers, artisans and other self-employed people) with different parameters, rules and regulations. A single public agency (the SSI) was formed to take charge of the public provision of social security coverage and (non-contributory) social assistance payments to the whole of society. Differing rules and regulations (such as eligibility conditions and pension benefits) applying to different working groups previously falling under the jurisdiction of different institutions were also harmonised to a great extent. The law stipulated that entitlement ages for women and men be gradually increased after 2036, to be equalised at 65 by 2048. Law No 5510 also set the replacement rate at 2 percentage points for every 360 days for which contributions had been paid (with the cap currently at 50%), regardless of the level of retiring individuals' lifetime earnings. Thus, the rate set was the same for everyone. Actual monthly pensions to be collected after retirement were calculated by multiplying the replacement rate by average wage/salary income earned prior to retirement. However, for workers whose average lifetime earnings were higher than the legal maximum, the actual monthly pension amount was calculated by multiplying the legal cap by the applicable replacement rate.

Reform initiatives introduced to deal with the rapidly growing pension deficits in Turkey, however, focused almost exclusively on expenditure-cutting measures such as replacement rate cuts, and increases to entitlement ages to postpone the collection of benefits. Revenue-increasing measures remained limited to relatively minor adjustments to the number of contributory days, completely avoiding any increases to contribution rates. This was due mostly to complaints from employers about the already high tax burden on the payrolls of registered workers, often backed by concerns about the international competitiveness of Turkish products. Concerns were also raised over the large informal sector, which jeopardised the competitiveness of the formal sector. In the end, Turkish policy-makers ruled out increases to contribution rates and chose to focus on measures to reduce unregistered employment as practically the only means of increasing contribution revenues – alas with limited success given the structural nature of informality in Turkey.

Between 2005 and 2015 the minimum pension (which covered a large percentage of the population) increased by 142%, while inflation was 122%. Although higher than the inflation rate, the increase did not match the growth in GDP. Indeed, whereas it was 1.25 times the minimum wage in 2005, it was no higher than it in 2015 (DISK, 2018). This indirectly reflected the persistent problem of income inequality in the country; following a slight betterment in the GINI index in the early years of the AKP government, it fluctuated around 0.40, the worst in EU, and more recently has started to worsen further.

As reforms are set to be implemented gradually, they had limited impact in reigning in increasing pension expenditure in the period from 2005 to 2015.

1.2 Healthcare

Starting from 2003, a healthcare reform programme was instituted, changing the financing and provision of healthcare services fundamentally. Initially, a gradual improvement in public health insurance coverage was made and those people deemed to be poor and without social security saw increased access to healthcare services. Then, in 2008, a comprehensive premium-based public health insurance system aimed at universal coverage was legislated for and was fully implemented in 2012. The new system was premium-based, and covered the entire population (as long as premiums were paid). Although the new system had a wider coverage with its mean-tested full subsidy for poor households, in 2014 it was announced that 7 million individuals, about 9% of the population, had failed to pay their premiums but could not pass the means-test either, and hence were without coverage (Bülbül, 2015).

Reforms have also provided access to private providers and improved service quality by public providers. This resulted in a sharp increase in the use of healthcare services. Per capita doctor visits increased to 8.4 in 2015 from 3.1 in 2002, and per capita hospital visits to 5.7 visits in 2015 from 1.9 in 2002 (MoH, 2016). Public health expenditure increased by 28% between 2005 and 2008 in real terms. After that, public health expenditure stabilised with the implementation of a new family physician service for primary care services, the introduction of co-payments for hospital visits and drugs, a sharp increase in charges allowed by private hospitals to insured patients, and the impact of global financial crisis; as a result it only increased by 5.6% between 2008 and 2015 in real terms. In the meantime, the share of out-of-pocket health expenditure in total health expenditure fell from 22.8% in 2005 to 16.6% in 2015,

An important area of health expenditure has been that for Syrian refugees. Deputy Prime Minister Mr. Recep Akdağ announced that between 2011 and the end of 2017 health-related expenditure by the government for Syrians exceeded 16 billion TL (€4.978 billion).[2]

Public health insurance subsidies and most social assistance programmes are means-tested in Turkey. Although the income threshold for most formal social assistance programmes is set as a per capita household income of less than one third of the gross minimum wage, assessment is in practice made through an investigation of a household's circumstances. Erus et al. (2015) found, from EU-SILC (European Union Statistics on Income and Living Conditions) data from 2007, that non-take-up was as high as 44% among those below the means-tested income threshold. The system has been improved over time, and a central database along with an automatic assessment system has been developed. That said, however, the system is open to various discretionary applications. The share of expenditure that was based on means-testing stayed stable at around 9% in the period 2005-2015.

1.3 Other spending

The increase in the share of spending on disabled, family, and social exclusion benefits between 2005 and 2015 reflected changes in social assistance programmes. Turkey lacks a minimum-income scheme. The social assistance system is patchy and fragmented. Though not instituted as a policy, the possibility of introducing minimum-income schemes

[2] https://tr.sputniknews.com/turkiye/201712061031278968-recep-akdag-suriyelilere-harcanan-para. A caveat is necessary, though: as we do not have the yearly breakdown of expenditure, we had no choice but to take the average TL/€ parity between 2011 and 2017. To what extent, if any, health expenditure has been co-financed by international agencies (the EU being the primary donor) is also not known.

in Turkey has been debated in both academic and policy circles during the last decade.[3] But currently, largely because of the ongoing crisis, there are no ongoing discussions either on eligibility conditions or on the level and duration of a minimum-income scheme. The announcement by the Ministry of Family and Social Policy (MFSS) during a parliamentary presentation in 2014 that work on a minimum-income scheme was about to be completed turned out to be incorrect.

In line with the intention to provide improved social assistance during the period 2005-2015, several social assistance programmes were put in place, and those already in place were improved. Regular social assistance programmes were instituted for certain groups, achieving a coverage of 2.3 million individuals. One for widowed women, for example, was introduced in 2011, under which a regular monthly payment was made to 290,000 women in 2016. The assistance programmes for elderly and disabled people were significantly improved, and reached more than 1.2 million individuals in 2016 with spending of 4.7 billion TL (€0.79 billion).[4] Expenditure on irregular in-cash and in-kind transfers, which benefited 2 million individuals in 2016, was increased. The government introduced a number of social assistance programmes, such as conditional cash transfer programmes, which have initially been run with support from the World Bank and have been continued since 2007 with government funding only.

Also notable was the increase in unemployment expenditure. In Turkey unemployment insurance was first implemented in 2000. Coverage is still rather limited due to informality in the economy, as only those who have been employed in formal jobs are entitled to unemployment insurance benefits. In 2018, 4.8 billion TL (€0.80 billion) was paid to unemployed people. As the number of beneficiaries, 577,054 individuals as of December 2018, has been rather low since 2003, a large fund has accumulated over time. Although the law initially restricted the use of this for other purposes, a later amendment allowed for the use of a given year's premium revenues for policies targeted at promoting employment, such as active labour market policies and employment in public works. As a result, the share of unemployment in social protection spending increased from 1.1% in 2010 to 1.9% in 2015.

A final point, which will be discussed below in detail, is the relatively low level of government revenue in the form of taxes, which creates pressure not to increase expenditure on social protection. The fact that the bulk of taxes is being collected by indirect taxes further complicates the problem, as it places a welfare cost on society.

[3] See Adaman et al. (2016) for a detailed exposition of legislative efforts and other aspects of minimum-income related schemes in Turkey.

[4] At 5.98 TL/€, the average exchange rate for February 2019.

2 Current mix and past changes in the sources of financing for social protection

Social contributions made up 52.3% of financing for social protection in 2015, followed by general government contributions (42%) and other receipts (5.7%). The health and pension systems are designed to be funded by social contributions: but government contributions are used to cover deficits in the pension system. Unemployment insurance had a surplus, with premiums exceeding outflows. Social assistance programmes are paid for out of government revenues.

Table 2: Division of financing for social protection by main source, Turkey, 2005-2015 (%)

	2005	2008	2010	2015
Social contributions	42.4	45.8	47.3	52.3
General government contributions	48.8	44.8	45.1	42.0
Other receipts	8.8	9.4	7.5	5.7

Source: Spasova and Ward (2019), Annex ESSPROS tables.

It should be noted that the composition of financing had changed compared with 2005, when social contributions had a lower share (42.4%) and government contributions a higher one (48.8%). The change was gradual, with the share of social contributions rising to 45.8% in 2008 and 47.3% in 2010. The fall in the share of general government contributions paused in the period 2008-2010, possibly as a result of government's fiscal policies to counter the effect of global financial crisis, as well as falling GDP.

A major reason for the rising share of social contributions was the reforms to retirement and healthcare. As noted in Section 1, the retirement reforms in 1999 and 2006 raised the retirement age and reduced pensions, thus bringing down the deficits in the system and the need for government contributions. In healthcare, the reforms brought in a universal health insurance system, and financing became heavily based on social contributions.

In 2015, around 50% of all social contributions fell on employers, 35% on employees, 11% on self-employed people, and 4% on benefit recipients (data on specific functions, such as pensions and healthcare, are lacking). The share of employers fell from around 56% in 2005. In contrast, the burden on self-employed people increased from about 9% to 16% between 2005 and 2008, before falling back. For employees there was a gradual increase over time, from around 33% in 2005.

As to the government contribution, that was heavily financed through general revenue in both 2005 and 2015, with earmarked taxes making up 1.8 and 1.5 percentage points of the total, respectively. The means-tested benefits made up 9.1 percent of the total in 2015 and their share was very similar to the one in 2005 of 8.9 percent.

As a separate issue, unemployment insurance is financed by premiums collected from employees (1% of gross monthly salary) and employers (2% of gross monthly salary). The government contribution is 1% of gross monthly salary.

2.1 Pensions

As noted above, the pension system has been running large deficits since the early 1990s despite two waves of reforms since then. According to SSI statistics, in 2015 social contributions covered 75.5% of total pension and health payments, and state contributions covered the rest.

The pension system is a PAYG scheme which is provided by the state to all workers and self-employed people. Participation is compulsory for all wage and salary earners as well as (in principle) self-employed individuals. The actual coverage is less comprehensive due to serious compliance problems. Although earnings are subject to income taxes

withheld at the source and calculated using progressive rates, ranging from 17% to 35%, social security contributions are not progressive. Contributions are calculated as a percentage of gross salary and are collected at fixed rates, currently standing at 9% for employees, and 11% for employers. Employers who do not owe any back-payments of contributions get 5 points off in the relevant month. The floor for the income subject to contributions is set at the minimum-wage level. The cap was set at 6.5 times the minimum wage until 2017 and then increased to 7.5 times.

Pensioners who take new jobs after retirement are subject to the so-called social security support premiums, collected at the rate of 30% (22.5% from employers and 7.5% from the pensioners).

The minimum number of contributory days for a worker to become eligible for retirement is 7,200 days (20 years) for private sector employees, and 9,000 days (25 years) for civil servants and self-employed workers. The minimum retirement age is 58 for women and 60 for men whose working life first started after the 1999 reform. Those who were already working in 1999 will be subject to a scheme gradually raising their retirement age, depending on their seniority at the time. Starting from 2036 the minimum retirement age for women and men will gradually increase, to reach 65 by 2048. However, there are early retirement options and relaxed conditions for part-time workers, miners, people deemed incapable of work, and disabled people.

Premiums also cover survivor benefits, which extend to spouses, children, and parents who qualify as dependants. Benefits consist of lump-sum payments, monthly payments, payments for funeral expenses, and payments to daughters when they get married. For the payments to be made, the deceased should have paid premiums for 1,800 days (900 is sufficient if they had been registered with the SSI for at least five years) or have already retired. Spouses are entitled to 50% of the pension calculated for the deceased (75% if there is no other person receiving survivor benefit and the spouse has no other income). Children are entitled to 25% of the benefit (50% if both mother and father are deceased). While there is an age limit of 18 for male children, female children are entitled to the payment as long as they are not married. There is no age limit for disabled people either.

The government contribution towards financing deficits in the retirement system is sizeable. Although it is expected to improve as the reforms of 1999 and 2006 are gradually implemented, the government took steps to reduce the dependence of individuals on public retirement benefits by introducing and incentivising private retirement plans. Since 2017, all employees younger than 45 are automatically enrolled in such plans and contribute 3% of their taxable earnings, with the possibility of opting out. As of March 2019, 6.8 million individuals were covered by a private policy.

2.2 Healthcare

The healthcare system is financed through premiums paid through a universal health insurance system. The government contribution is limited to payment of premiums for those deemed unable to pay, based on a means-testing procedure. Employees registered with the SSI have premiums of 12.5% of their reported income, of which 7.5 percentage points is paid by the employer. For the registered self-employed, the premium is paid directly by the insuree. Premiums cover dependants as well. Those younger than 18 are automatically covered as long as they are registered in the system, even if their parents are not insured. Students are covered as dependants if their parents are insured while they are studying, and also for two years following their graduation as long as they are younger than 20 (for high school) or 25 (for university). Satisfaction with health services increased dramatically following the reforms, from 39.5% in 2003 to 75.4% in 2016. That being said, public providers have waiting times, especially in diagnostics and surgery, and charges by private providers are difficult to afford for low-income households. Also problematic are provider payment systems that incentivise quantity at the expense of the quality of healthcare.

The self-employed often fail to pay their social security contributions. Alper (2011) reported that only 44% of self-employed people in non-agricultural activities (previously covered by Law No 1479) were fully up to date with their contribution payments, whereas 33% were in arrears with their contributions, and the remaining 23% had never paid any contributions after registering themselves. The same percentages were 52%, 30% and 18%, respectively, for people working on their own account in agriculture.

The public health insurance system was legislated for in 2008 and, in its original form, the premiums for unemployed and informal workers without social security coverage depended on household income. Until 2017, there used to be three levels of premiums based on monthly household income, going up to 426.60 TL (€71) for those with household per capita income higher than two times the gross minimum wage. Those who did not apply for means-testing were automatically assigned the highest income level and paid the highest premiums. Facing a large number of people on the highest premium level because of this, and facing difficulty in collecting premiums, the government changed the system in 2017 and set the monthly premium at 60.88 TL (€10) for those who did not have social security coverage through their employment and who did not qualify for government assistance. For low-income households, defined as those with per capita household income of less than one third of the gross minimum wage, premiums were paid by the government.

Insurees have to pay additional fees (user fees) for the services they utilise. A user fee is paid for outpatient clinic services (except for family physician visits), medication prescribed in outpatient clinics, prosthetic and orthetic aids, and in vitro fertilisation (IVF) services. Additionally, in the case of attendance at secondary and tertiary healthcare services, a user fee is charged. These fees were implemented from 2009, stayed the same for 7 years, and were then increased by 20-25% in 2017. The charge is 6 TL (€1) for using public providers and 15 TL (€2.50) for private ones.

2.3 Major issues

Two structural problems related to the issue of financing social protection need to be raised. The first one is the relatively low share of employed people in the entire population. On the one hand, the low labour force participation rate (fluctuating around 50%) has mainly been due to the low participation rate of females (fluctuating around 30%). On the other hand, the unemployment rate has been high (fluctuating around 10%). Putting the two together indicates that the dependency ratio is high, increasing the likelihood of poverty among households – thus creating difficulties for the government in financing their health and other related social expenses.

The second problem is the high prevalence of informality. It is known that approximately 1 out of every 3 working people is unregistered (Başlevent and Acar, 2015). Although informal employment in Turkey declined by around 15 percentage points between 2002 and 2015, it was still quite high, and as such it harmed the sustainability of the social security system due to diminished premium and tax revenues. The ratio of tax revenues to GDP in Turkey in the period concerned was around 25% (which was well below the EU average of 40%). In passing, one should also note that the bulk of tax revenues (around 65%) consisted of indirect taxes, which brings about serious welfare implications for society. So far, the informality issue has not been addressed from a structural point of view. Only recently has government policy to incentivise job creation been instrumental in reducing the scale of informality – and the effect is so far rather small.

3 Strengths and weaknesses of the existing mix of financing options and potential future sources of financing - national debate on the topic

As discussed earlier, the pension and health systems in Turkey are insurance-based. However, due to populist policies on pensions in the 1990s (in the sense of reducing the retirement age without regard to the long-run financial sustainability of the system), the system is still in deficit – despite reforms in 1999 and 2005 aimed at addressing the problem by increasing the entitlement (retirement) age and reducing pension benefits.

Apart from the impact of earlier populist policies, there are serious weaknesses in the system that are mainly driven by structural problems in Turkey's political economy. The first and most important one is the prevalence of informality: apart from evasion, which puts a heavy financial burden on the formal sector, informality brings about additional costs, such as unfairness, erosion of trust in the system, and social costs for the uncovered labour force. Additionally, as some of the informal sector is on a small scale, thus under the radar of any regulatory bodies, informality is usually associated with unsafe working conditions and environmentally damaging activities. The fact that some work accidents are not reported officially (but negotiated between the parties) speaks for itself.

Unregistered employment should be combated seriously, not only through such measures as better and more effective inspection and higher fines, but also by directly tackling the underlying causes of unregistered employment, ranging from the low education and skill levels of the workforce to small firm size.

The second structural issue is low labour force participation, which is due to the female rate fluctuating around 30% – the lowest in the OECD countries.[5] This is yet another reason behind the imbalance between premium revenues and pension benefits. Apart from the lack of affordable childcare, which is especially acute in the informal sector, it is also evident that poorly educated women continue to face serious cultural barriers that constrain their participation (World Bank, 2009).

In addition, thirdly, unemployment has been an acute structural problem. As mentioned above, the rate fluctuated at around 10%, rising further during the years of crisis. This undoubtedly places a financial burden on the system. The problem is multifaceted, but the low level of human capital must perhaps be singled out. Attention should perhaps also be paid to conditions in the agricultural sector. Currently holding approximately one fifth of the working population, the agricultural sector has been in disarray during the last three decades, creating a huge push factor, which in turn creates unemployment (Keyder and Yenal, 2011). A final point to be added is the fact that the inflow of Syrian refugees, totally almost 2.5 million by the end of 2015, aggravated the problem, as they were ready to work in the informal sector for much lower wages.

In all these three aspects, human capital emerges as a key component. Apart from the low levels of enrolment in education, the system faces a serious quality problem as well. With the exception of a small percentage of educational institutions (from kindergartens to universities), the overall quality is far behind satisfactory levels.

These three issues lead to a low number of active contributors per retiree or survivor. Under these circumstances, although social security premiums are criticised for being too high and creating a burden on employers as well as employees, the government has no space to ease the burden.

As described above, the contribution system is not progressive. The rate is the same at all incomes up to the cap. The effective rate of premiums is lowered by widespread informal working, and by the fact that employees are able to hide their incomes –

[5] https://stats.oecd.org/Index.aspx?DataSetCode=LFS_SEXAGE_I_R.

reporting income at the minimum wage level but actually receiving more than that. In 2012, during discussions on setting the minimum wage, the Minister of Finance of the time, Mr. Şimşek, said that 55% of the 5 million individuals who appeared in the records of the SSI under-reported their income.

Furthermore, ongoing deficits financed by the government rely on general tax revenues, which are not essentially progressive. While income taxes are collected at increasing rates as income goes up, most tax revenues come from indirect taxes, as mentioned above. It is likely that this structure puts a relatively heavier burden on poorer households compared with a progressive and functional tax system (see Zenginobuz et al. 2010 for a detailed analysis).

The age limits set by the reforms of 1999 and 2005 will gradually raise the retirement age to 65. However, there is pressure on political parties to remove the age limit, by those who have completed the minimum number of days required for retirement but are younger than the minimum required age. Known as 'Emeklilikte Yaşa Takılanlar' (Those Trapped at the Age Requirement), a large group of individuals have been conducting social media campaigns to prompt the legislative work to be undertaken. Although they have so far failed to force a legislative change, a proposal has been made for a parliamentary discussion session by opposition parties. The proposition was rejected by the government. While removal of the age limit would be catastrophic for the finances of the pension system, it is also the case that, given the high level of unemployment, for many people it is difficult to stay employed until old age.

In healthcare there are two major concerns about the system. First, it has been argued that the public health insurance subsidy, which covers about 10% of the population, encourages informal employment. The MFLSS has been working since 2013 to sever the link between social assistance programmes and employment. Starting in 2018, all 'employable' social assistance beneficiaries have to register with the public employment service, İŞKUR. Assistance is stopped for one year if the beneficiary refuses participation in active labour market training programmes or job offers by İŞKUR. There is also a subsidy to employers who employ someone on the social assistance rolls.

The second concern is enforcing premium payment, especially among self-employed people. Unlike salaried workers whose premium is automatically deducted, self-employed people are responsible for making payments by themselves. Lack of compliance is widespread and resulted in an amnesty in 2014. The late fees and interest charges on unpaid premiums were cancelled, and premiums were to be paid in at most 18 instalments. Subsequently, a further legal amendment froze the debts of a specific group of uninsured people, composed mainly of rural and self-employed people. About 7 million individuals were expected to benefit. That said, Erus et al. (2015) found that a considerable proportion of the poorer population is without health insurance. Such a significant weakness in the system ends with inequality in access to healthcare and the utilisation of health services, or with significant out-of-pocket payments that are particularly detrimental for poor households.

It should finally be noted that although health insurance premiums are enough to cover the costs of the system, with a slowing economy and increasing healthcare and drug prices, financial problems are likely to arise in the future.

Among the issues that may arise in the near future is that of financing the burden created by the huge inflow of Syrian refugees. In addition to its adverse impact on the labour market, as touched upon above, supporting a large population in poverty constrains the government budget.

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