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Article

# Social expenditure and the politics of redistribution

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**Summary** This article offers a critique and analysis of recent OECD research by Adema and Ladaique identifying the impact of taxes and private benefits on social spending. By using the techniques of multivariate modelling, we show that both gross public and net private expenditures are strongly influenced by partisan incumbency, although in opposite directions, and that the more we net out the effect of taxes, the less politics matters and the more spending is shaped by socio-economic forces. In a second stage of the analysis, we show that the crucial mechanism of welfare state redistribution is the taxation of gross social expenditure and demonstrate that this effect is almost entirely political in nature.

**Key words** net social expenditures, politics matters, redistributive policies, socio-economic explanations, tax incidence,

## Introduction

Almost certainly, the most comprehensively studied field of comparative public policy has been the welfare state. The major reason that the study of social policy outcomes has been so appealing to scholars was, undoubtedly, the early availability of cross-national, welfare expenditure data compiled by international organizations such as the ILO and the OECD. Despite its popularity, however, such research has been strongly critiqued from the outset. Quite apart from obvious difficulties resulting from the limited reliability of cross-national spending data and inconsistent time-series, it has also been suggested that social expenditure is 'epiphenomenal to the theoretical substance of welfare states' (Esping-Andersen, 1990: 19–20). More specifically, it has been argued that expenditure can neither identify and measure the redistributive effects of social programmes, nor shed light on real outcomes for welfare clienteles, which are far better captured by information concerning qualifying conditions, programme coverage and benefit replacement rates. Expenditure-based studies relying on publicly provided data about publicly provided programmes have also been blamed for a tendency on the part of scholars to ignore both the incidence and outcomes of private provision. In a nutshell, public expenditure by itself has been widely seen as an insufficient basis for providing a nuanced account of welfare provision or identifying its effects (Castles, 1993: 350).

However, both data availability and comparability have improved very considerably over the past decade with the publication of the OECD Social Expenditure Database (SOCX). This dataset disaggregates social expenditure into a series of what were originally 13, but in the most recent version

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(OECD, 2004) nine, components of spending and numerous separate programme headings for all the long-term member countries of the OECD from 1980 onwards, permitting far more detailed analysis of cross-national spending profiles than ever before (see Castles, 2004). Despite these improvements, the dataset can still be criticized because it does not adjust expenditure to take account of the potentially distorting effects of diverse tax policy regimes and cross-nationally distinct public–private mixes. Some countries tax social benefits, while others do not. Some mandate employers to pay benefits to workers that would elsewhere be directly provided by the state. Some offer tax relief to encourage individuals to contribute to privately run schemes, while others scrupulously avoid such interventions. Finally, in some countries, spending on private welfare schemes is much higher than in others. The result is that the quantum of welfare provided to individuals in a given society corresponds only very loosely with the gross expenditure figures reported in budget documents, National Accounts statistics and the datasets produced by international organizations such as the OECD.

For some time, the OECD has been attempting to overcome these difficulties by providing information on net (after tax) public and private social expenditure for an increasingly large number of member states. In the latest adumbration of this important research effort, Adema and Ladaique (2005) seek 'to elaborate more comprehensive measures of social support' by taking into account the impact of taxes and private spending in a group of countries now numbering more than 20. Key findings of this study are that cross-national variance in net spending is far less than in respect of the more usually compared gross public expenditure measure; and that the shift to net social expenditure figures leads to remarkable changes in the reported relative magnitudes of welfare spending across the OECD world. The authors claim that, in contrast to gross spending figures, their '*net current public social expenditure* indicator . . . provides a picture of what governments "really" devote to social spending' and that their measure of *net current total social expenditure* (which includes private benefits) 'allows [us] to assess what part of an economy's domestic production recipients of social benefits draw on' (Adema and Ladaique, 2005: 6). It would seem, then, governments and economists have reasons to be as interested – or even more interested – in cross-national comparisons of net than of gross spending.

The underlying purpose of this article is to ask whether a similar conclusion holds for students of public policy and those concerned with the redistributive impact of social spending. In particular, we seek to establish whether changes in cross-national spending relativities resulting from these new ways of measuring expenditure have any consequences for the explanatory power of the main schools of thought in comparative public policy analysis. Much of our knowledge concerning the political and socio-economic determinants of the welfare state rests on the analysis of gross social expenditure, and much of our understanding of the purposes of the welfare state rests on assumptions about linkages between gross expenditures and redistributive policy outcomes. Given a much greater similarity in net spending levels across countries, it is important to investigate whether the main bodies of theory in comparative public policy analysis remain relevant in accounting for cross-national variation in net expenditures and whether the link between net expenditures and outcomes resembles that between gross spending and outcomes. The inclusion of voluntary private spending data in the OECD study also opens up the question of whether established theoretical paradigms can illuminate cross-national differences in public–private mixes in welfare state provision in the advanced OECD countries.

The fact that data on net spending are now available for a sizeable number of countries makes it possible for us to use multivariate regression analysis and other simple statistical techniques to provide preliminary answers to these questions. The results are striking, pointing to the crucial importance of economic factors in shaping net expenditure levels, and possibly suggesting the need for a reappraisal of once dominant, but no longer fashionable, functionalist accounts of social expenditure development. Although our analysis suggests that partisanship plays no part in explaining total net social expenditure levels, we find evidence that it is an extremely powerful factor in accounting for the nature of the public–private mix in social policy. We also note interesting findings in respect of the impact of political institutions and the timing of welfare state consolidation, the latter indicative of a moderately strong path dependency effect on postwar expenditure development. Finally, we show that much of the redistribution affected by

welfare states is a function of the incidence of taxation on benefit expenditure, which is only fully captured in measures of gross expenditure and which is almost entirely politically determined. Because we regard such redistributive outcomes as being central to the theoretical substance of welfare states, we question whether these new measures of net spending 'really' do tell us more than the measures of gross spending they are seen as superseding.

The remainder of the article is organized as follows. We start by providing a brief overview of net social expenditure figures and investigate the extent to which the cross-national relativities they reveal differ from those familiar from research on gross expenditure levels. Next, we analyse the determinants of expenditure levels variously including or excluding the impact of taxes, mandatory expenditures and private spending. Starting with the analysis of gross expenditure and using the same set of independent variables, we extend the analysis to various categories of net social expenditure, including, finally, expenditures net of both taxes and private spending. We complete our analysis by demonstrating that the extent of taxation on gross spending is a crucial predictor of the redistributive impact of the welfare state and that this taxation effect is strongly shaped by the partisan complexion of government. The final section concludes with an afterword.

## The data

Since its first publication in the mid-1990s, the OECD Social Expenditure Database has increasingly been the data source of choice for most comparative research relating to the welfare state. This source provides disaggregated data on gross social expenditure and its component programmes dating back to 1980 for all the long-term OECD member states. Unfortunately, however, the dataset does not provide information concerning cross-national differences in the impact of tax policy on social expenditure, the extent of benefits mandated by, but not provided by, the state and the quantum of voluntary private social spending. At a minimum, this means that our understanding of the cross-national relativities of social spending is incomplete. Arguably, it also suggests that the prevailing understanding is distorted.

Tax policy effects on social expenditure are of two kinds (Adema and Ladaique, 2005: 15–16). First, governments can levy taxes and social security contributions on transfer payments and/or may levy indirect taxes on goods and services bought by the recipients of such transfers. Second, governments can provide tax breaks for social purposes of a kind equivalent to cash benefits (as, for instance, the increasing use of child tax benefits and low-income tax benefits) as well as to encourage the private acquisition of functional equivalents to cash benefits (e.g. private pensions or health insurance). Relevant to our later discussion, it should be noted that the distributive effects of these kinds of tax intervention may well be quite different. Direct taxes on benefits involve clawing back income from the well-off, and social security contributions, while often not proportional right across the income distribution, generally mean that those with higher earnings contribute more than those with lower earnings. Again, indirect tax is not always proportional to income, but clearly those with larger earnings-related benefits are likely to be paying more tax than those with lower flat-rate benefits. Yet, while tax breaks in the form of tax credits to those on low incomes are explicitly redistributive in intent, tax incentives to private expenditure are generally taken up disproportionately by those on high incomes. Thus, the overall impact of tax breaks is less clear than tax interventions of the first type, with the outcome dependent on the particular balance between tax breaks favouring different income classes. However, given that, for the group of OECD countries analysed here, interventions of the first type outweigh those of the second type by a margin of 3.3–0.5 percent of GDP (calculated from Adema and Ladaique, 2005, Table Annex 3: 71), the presumption must be that overall tax effects are likely to be decidedly redistributive in character.

The Adema and Ladaique study (2005) nets out all tax effects of both the first and second type to move from a category of *gross public social expenditure* to one of *net current public social expenditure*. The study also estimates the extent of *net current private social expenditure* by summing the quantum of mandatory and voluntary private social expenditure in each country, once again netting out the effects of both direct and indirect taxes. The study adds together net current public and private expenditures, and arrives at a figure for *net total social expenditure* which, as already noted, is seen as constituting 'that proportion of an economy's domestic production to which recipients of social benefits lay claim' (Adema and Ladaique, 2005: 30).

**Table 1** Social expenditure as a percentage of GDP (at market prices) in 2001

| | *(1) Gross public social expenditure* | *Rank* | *(2) Net current public social expenditure* | *Rank* | *(3) Net current private social expenditure* | *Rank* | *(4) Net current total social expenditure (2+3)** | *Rank* |
|---|---|---|---|---|---|---|---|---|
| Australia | 18.00 | 14 | 17.10 | 13 | 4.20 | 3 | 21.10 | 11 |
| Austria | 26.00 | 5 | 20.60 | 7 | 1.20 | 12 | 21.80 | 10 |
| Belgium | 24.70 | 7 | 21.20 | 5 | 2.00 | 9 | 23.20 | 5 |
| Canada | 17.80 | 15 | 17.10 | 13 | 3.50 | 5 | 20.30 | 13 |
| Denmark | 29.20 | 2 | 21.80 | 4 | .70 | 15 | 22.50 | 7 |
| Finland | 24.80 | 6 | 19.20 | 10 | .70 | 15 | 20.00 | 15 |
| France | 28.50 | 3 | 25.20 | 2 | 1.80 | 10 | 27.00 | 2 |
| Germany | 27.40 | 4 | 25.40 | 1 | 2.60 | 7 | 27.60 | 1 |
| Ireland | 13.80 | 18 | 12.20 | 18 | .40 | 17 | 12.40 | 18 |
| Italy | 24.40 | 8 | 20.90 | 6 | 1.20 | 12 | 21.90 | 9 |
| Japan | 16.90 | 16 | 17.10 | 13 | 3.20 | 6 | 20.20 | 14 |
| Netherlands | 21.40 | 11 | 18.00 | 11 | 4.50 | 2 | 22.10 | 8 |
| New Zealand | 18.50 | 13 | 15.50 | 17 | .50 | 16 | 15.90 | 17 |
| Norway | 23.90 | 9 | 19.60 | 9 | 1.20 | 12 | 20.90 | 12 |
| Spain | 19.60 | 12 | 16.70 | 15 | .30 | 18 | 17.00 | 16 |
| Sweden | 29.80 | 1 | 23.70 | 3 | 2.20 | 8 | 26.00 | 3 |
| UK | 21.80 | 10 | 19.80 | 8 | 3.60 | 4 | 23.30 | 4 |
| USA | 14.70 | 17 | 15.90 | 16 | 8.50 | 1 | 23.10 | 6 |
| Mean | 22.29 | | 19.28 | | 2.35 | | 21.46 | |
| SD | 4.98 | | 3.47 | | 2.04 | | 3.74 | |
| Range | 16.00 | | 13.20 | | 8.20 | | 15.20 | |
| CV | .22 | | .18 | | .87 | | .17 | |
| Mean Scandinavian[a] | 26.92 | | 21.07 | | 1.20 | | 22.35 | |
| Mean Continental[b] | 25.6 | | 22.08 | | 2.42 | | 24.34 | |
| Mean English-speaking[c] | 17.43 | | 16.27 | | 3.45 | | 19.35 | |

*Notes*:
[a] Scandinavian family of nations: Denmark, Finland, Sweden and Norway.
[b] Continental family of nations: Austria, Belgium, France, Germany and the Netherlands.
[c] English-speaking family of nations: Australia, Canada, Ireland, New Zealand, the UK and the US.
[d] Some of the figures in Column (4) are somewhat smaller than would be indicated by the equation: (4) = (2) + (3), since, in order to avoid double counting, Adema and Ladaique deduct tax benefits towards current private benefits from this total in countries where such tax benefits exist.
*Source:* Data are taken from Adema and Ladaique (2005: 71).

**Table 2** Correlations between different categories of social spending

| | *Gross public social expenditure* | *Net current public social expenditure* | *Net current private social expenditure* |
|---|---|---|---|
| Net current public social expenditure | .920* | | |
| Net current private social expenditure | –.382 | –.133 | |
| Net current total social expenditure | .689* | .881* | .350 |

*Note*: Pearson correlation coefficient. Significant correlations are denoted by an asterisk.

The study estimates spending under these headings for 23 countries in the year 2001. Table 1 reports data for 18 of these countries selected variously on the basis of the availability of full information on these spending measures and of data for the independent variables featuring in our analysis. The expenditure figures reported in Table 1 are related to GDP at market prices (Adema and Ladaique, 2005: 71), although the Adema and Ladaique study itself prefers comparisons at factor cost (Adema and Ladaique, 2005: 32). We use market price estimates because we are interested in comparisons with gross expenditure levels, which typically are expressed as percentages of GDP at market prices.

Table 1 presents a simplified version of Adema and Ladaique's findings for 18 long-term OECD countries. Column 1 reports gross public social expenditure and various categories of net spending are reported in Columns 2–4. The table also includes rankings for each of the four variables. The rankings make it simple to identify the striking changes which occur as we move across the columns from gross public to total net expenditure. Countries such as the US and the UK, traditionally regarded as 'residual' or 'liberal' welfare regimes, increasingly appear in the spending vanguard once taxes are netted out, and once private social expenditures are taken into account. Whereas the majority of English-speaking countries and continental Western European countries are ranked higher in terms of total net social expenditure, the Social Democratic welfare states of Scandinavia move downward in the international net spending league. As a result, average levels of total net social spending for the three families of nations reported in the summary statistics section of Table 1 are markedly more similar than in respect of gross expenditure. Equally, as we move towards more netted and more inclusive measures of total spending, coefficients of variation decline appreciably. These figures suggest that the major dividing line between the different welfare state regimes or families of nations is defined less by the extent of the total welfare effort and rather more by differences in the public–private mix of benefit provision typical of these groups of countries. Private spending in the English-speaking world is almost three times higher than in Scandinavia. Conversely, looking at the difference between Columns 1 and 2, we can see that the incidence of taxation on social spending in the English-speaking world is significantly lower than in either of the other two families of nations.

Table 2 reports correlations between the four spending measures presented in Table 1. The fact that the correlation between net current private spending and the gross expenditure category is negative strongly suggests that public and private spending are, in some measure, substitutes for one another. This, in turn, implies that a neglect of private spending does, at least to some extent, distort our understanding of overall welfare state effort. In contrast, the impact of taxation on cross-national patterns of social spending would appear to be rather more limited, since the correlation between gross and net public spending is extremely strong. As we shall point out subsequently, however, the redistributive effects of taxation are rather more pronounced than this correspondence of spending categories might seem to indicate.

## Determinants of gross and net social expenditure

In this section, we examine whether or not the main schools of thought of comparative public policy research account for the cross-national variance of the measures of gross and net social expenditure reported in Table 1. These bodies of theory, the predictions they generate, and the ways in which they are measured in this article are summarized in Table

3. More elaborated discussions of these theoretical accounts can be found in Wilensky (1975), Skocpol and Amenta (1986), Schmidt (1996), Castles (1998), Huber and Stephens (2001) and Myles and Quadagno (2002). The hypothesis from which we initially proceed is that the impact of politics is likely to decline as the focus moves from gross to net social expenditure. The underlying rationale is that politics has a well-documented influence on the incidence of taxation that is likely to disappear if after-tax spending is analysed.

Since data on net social expenditure are available for 2001 only, we have to restrict ourselves to the analysis of the determinants of expenditure levels at that date. Given the 'tyranny of past political commitments' typical for public spending (Tanzi and Schuknecht, 2000: 20), and paraphrasing the metaphor which Lipset and Rokkan (1967) used to describe party systems and voter alignments, we interpret present-day social spending levels as being substantially the 'frozen landscapes' of political and economic circumstances in the past. More specifically, we explain cross-national variation in spending levels in 2001 largely as a legacy of the development of the political economy over the course of the postwar era. Hence, with the exception of the economic growth variable (which averages data only for the two decades prior to the turn of the millennium) and the social need index (which identifies the extent of need at the point of our 2001 expenditure measurement), our other indicators are long-term averages or proxies for historical particularities (the adoption of programmes or constitutional structures) dating back to 1950 or earlier.

Although substantial improvements in country coverage have been achieved in the latest version of the net expenditure dataset, data are still missing for a number of the longer-term OECD member states for which we possess full information for our chosen independent variables. This means that we must exclude Switzerland, Greece and Portugal, along with a number of new member states (the Czech and Slovak Republics along with Korea and Mexico) for which the required independent variable data are not available. We also exclude Iceland on grounds of small population size, leaving only the 18 countries featuring in Table 1 as the cases for the regression analysis which follows. In order to guarantee the comparability of the findings of that analysis, we use the same set of independent variables to model all four of the categories of social expenditure identified in Table 1; that is, gross public social expenditure, net current public social expenditure, net current private social expenditure and net total social expenditure.

We report five models for each category of spending. A baseline model consists of three variables. They are the level of GDP per capita over the postwar period (1960–2001), the average rate of economic growth in the 20 years preceding the year in which expenditure levels are measured and the average degree of bourgeois party cabinet incumbency over the 1950–2000 period. The way in which the bourgeois incumbency variable is operationalized here makes it virtually the mirror image of Left incumbency and we see no need to elaborate separate models to test the impact of the latter variable – all that is required is to reverse the signs. This baseline model is then augmented by variables chosen from the most influential bodies of theory described in Table 3. In particular, we examine the impact of social needs, the timing of welfare state consolidation and the effect of political institutions on social expenditure. The potential explanatory significance of these variables is emphasized by numerous scholars of social expenditure development (e.g. Wilensky, 1975; Schmidt, 1996; Huber and Stephens, 2001; Castles, 2004). Finally, we report best-fit models containing only statistically significant terms. Given the relatively small number of cases featuring in the analysis, we felt it inappropriate to include more than four variables in any of our models. A correlation matrix for all the independent variables is to be found in the Appendix and suggests a negligible risk of multicollinearity among the variables. The strongest correlation is that between economic growth and the social need index [r = –.574].

Our point of reference is the analysis of *gross public social expenditure*. Table 4 summarizes our empirical findings. The estimated effects are compatible with the vast body of empirical research on the determinants of social expenditure in recent decades. All equations lend strong support to the 'parties matter' school of thought. The estimated coefficient for the bourgeois incumbency term is negative and highly significant, suggesting that social spending is strongly constrained under circumstances of prolonged bourgeois rule. Although unreported here, findings for the impact of Left

**Table 3** Major schools of thought in comparative public policy analysis

| *Theory* | *Indicator and predicted impact* | *Measurement* | *Data source* |
|---|---|---|---|
| Theories of socio-economic development | Underlying long-term functionalist imperative: expenditure positively influenced by economic affluence. | GDP per capita (1960–2001) in Geary-Khamis Dollars (average) | Maddison (2003) |
| | Short-term functionalist imperative: socio-economic problem pressure leads to an increase in social spending. | Social need index 2001 = 2* share of the elderly (65+)as a pct. of total population / country maximum + unemployment rate / country maximum. This weighting reflects the fact that the share of the elderly has an impact on two major welfare state programmes (pensions and health). | OECD Labour Force Statistics (2003) |
| | Variant combining measurement and problem pressure elements (see discussion below): expenditure varies negatively with recent rate of economic growth. | Economic growth (1981–2001) | OECD Economic Outlook (various years) |
| Power resources theory | Partisan complexion of government. Public expenditures vary negatively with bourgeois partisan control and positively with Left party strength. For private expenditures, the predictions are reversed. | Cabinet seats of bourgeois parties (1950–2000 [average]). Liberal, secular-conservative, ultra-Right, Christian Democratic and secular centre parties are classified as bourgeois parties. The partisan complexion of government for Spain refers to the post-democratization period. | Schmidt (2001) |
| Political institutionalism | Constitutional rigidities. The higher the number of constitutional veto points, the lower the spending. | Index of federalism, bicameralism and constitutional rigidity. | Lijphart (1999) |
| Theories of path-dependence | Temporal consolidation of the welfare state. The earlier that programmes are established, the higher the level of spending. | Average year when four social security programmes (occupational injuries, health insurance, pension and unemployment insurance) were adopted at the national level (or nationwide). | Schmidt (2005: 182) |

parties suggest that they have an equal and opposite positive effect on gross public expenditure levels. We also find evidence that the timing of welfare state consolidation is important for explaining gross spending. This variable serves as a proxy for the degree of maturation of social programmes, with a link between maturity and higher levels of spending arguably compatible with both functionalist and 'politics matters' accounts (see Wilensky, 1975; Schmidt, 2005). The negative sign of the reported

**Table 4** Determinants of gross public social expenditure (2001)

| | *1a* | *2a* | *3a* | *4a* | *5a* |
|---|---|---|---|---|---|
| Intercept | 37.63*** | 35.99** | 285.59*** | 37.57*** | 269.38*** |
| | (7.23) | (2.79) | (3.42) | (7.12) | (3.33) |
| GDP per capita (1960–2001) | 2.82E-005 | 6.33E-005 | 2.31E-004 | 9.19E-005 | – |
| | (.09) | (.15) | (.88) | (.28) | |
| GDP growth (1981–2001) | –3.34*** | –3.21** | –3.06*** | –3.38*** | –3.32*** |
| | (3.84) | (2.45) | (4.36) | (3.81) | (5.23) |
| Bourgeois Cabinet seats (1950–2000) | –.10*** | –.10*** | –.068** | –.096** | –.065** |
| | (3.51) | (3.36) | (2.55) | (2.90) | (2.46) |
| Social need index 2001 | – | .35 | – | – | – |
| | | (.13) | | | |
| Temporal consolidation of the | – | – | –.13** | – | –.12** |
| welfare state | | – | (2.97) | – | (2.86) |
| Index of federalism, | – | – | – | –.752 | |
| bicameralism and | | | | (.74) | |
| constitutional rigidity | | | | | |
| N | 18 | 18 | 18 | 18 | 18 |
| Adjusted $R^2$ | .73 | .71 | .83 | .72 | .83 |

*Notes*: Unstandardized regression coefficients; t-statistics in parentheses. * $p \leq .10$; ** $p \leq .05$; *** $p \leq .01$.

coefficient in Table 4 strongly supports the hypothesis, indicating that levels of contemporary spending are significantly lower in countries which adopted their programmes most recently. The one political variable not to feature as a significant predictor of expenditure outcomes is the number of constitutional veto points, although the coefficient for this variable is negative as suggested by the literature.

The estimated impacts of the three variables measuring socio-economic development are also largely in accordance with the conclusions of the recent literature on welfare state spending. An earlier generation of functionalist accounts suggested that social expenditure was, over the long term, largely a reflection of a country's level of economic development as measured by GDP per capita and, more immediately, a function of a country's level of need, with the effects of population ageing and unemployment, the two key factors generally identified in the literature. However, in most recent studies, these relationships are seen as having been superseded by political and institutional effects. The regressions reported in Table 4 do not reveal any significant impact of the level of economic affluence[1] or of our index of social need.

However, Table 4 does identify a strong negative relationship between social spending levels in 2001 and economic growth in the preceding two decades. This relationship confirms the findings of numerous pooled time-series regressions of postwar spending as well as the most recent cross-sectional analysis of Castles (2006: 50–1) and can be attributed to several factors. First, economic growth clearly has an endogenous effect on social expenditure growth as the determinant of the denominator of the expenditure to GDP ratio. Rapid GDP growth necessarily leads, all other things being equal, to a decline in the spending ratio and low growth to an increase in measured spending.[2] Although we are here discussing levels rather than the growth of expenditure, there is every reason to suppose that marked growth rate variation will impact on expenditure levels over periods as long as one or two decades. Second, high economic growth rates provide an ideal environment for policymakers seeking to restrain spending as a percentage of GDP. The Irish economic miracle of the 1990s is a case in point; so too was the Japanese economic miracle of the early postwar decades. Both demonstrate that high and sustained levels of economic growth permit finance ministers to pull off the ultimate conjuring trick of cutting the expenditure/GDP ratio while presiding over long-term increases in real expenditure. Finally, economic growth also impacts on the numerator of the dependent variable, with low growth typically associated with higher levels of unemployment and

**Table 5** Determinants of net current public social expenditure

| | *1b* | *2b* | *3b* | *4b* | *5b* |
|---|---|---|---|---|---|
| Intercept | 27.71*** | 15.56 | 215.33** | 27.70*** | 203.99*** |
| | (6.29) | (1.51) | (2.85) | (6.08) | (3.30) |
| GDP per capita (1960–2001) | 9.86E-05 | 3.71E-04 | 2.523E-04 | 7.58E-05 | – |
| | (.37) | (1.11) | (1.07) | (.26) | |
| GDP growth (1981–2001) | –2.82*** | –1.84[b] | –2.62*** | –2.81*** | –2.93*** |
| | (3.83) | (–1.75) | (4.11) | (3.68) | (5.46) |
| Bourgeois Cabinet seats | –.035 | –.040 | –.0080 | –.038 | – |
| (1950–2000) | (1.40) | (1.63) | (.33) | (1.37) | |
| Social need index 2001 | – | 2.72 | – | – | – |
| | | (1.30) | | | |
| Temporal consolidation | – | – | –.10** | | –.092** |
| of the welfare state | | | (2.48) | – | (2.85) |
| Index of federalism, | – | – | – | .27 | |
| bicameralism and | | | | (.31) | – |
| constitutional rigidity | | | | | |
| N | 18 | 18 | 18 | 18 | 18 |
| Adjusted $R^2$ | .61 | .62 | .71 | .58 | .73 |

*Notes*:
[a] Unstandardized regression coefficients; t-statistics in parentheses. * $p \leq .10$; ** $p \leq .05$; *** $p \leq .01$.
[b] level of significance is .103.

higher growth permitting nations more easily to overcome the expenditure problems of an ageing society (see Schulz, 2002). This suggests that the economic growth variable may well be, to some degree, a surrogate for the extent of social needs, a surmise supported by the significant bivariate relationship between these variables reported in the Appendix table, and by the fact that, if the growth term is removed from Equation 2a in Table 4, the needs index becomes a statistically significant predictor of gross expenditure levels.

Having substantially replicated the conventional wisdom of a literature hitherto based exclusively on gross spending data, we now seek to take into account the impact of the tax system on cross-country spending levels by analysing the determinants of *net public social expenditure*. The results are presented in Table 5. With one hugely significant exception, the findings resemble those of Table 4 in that economic growth and temporal consolidation retain their significant negative coefficients, and levels of economic development, the index of social need and veto points (now actually marginally positively related to spending) remain insignificant. That there should be resemblances between the models comes as no real surprise, given the high correlation between gross and net public spending (see Table 2). The one really big difference between the models, however, is the absence of any partisan effects on after-tax public social expenditure. Even though the coefficient for bourgeois incumbency shows the expected negative sign, the story of the models in Table 5 is that, for net public spending, politics no longer matters.

An obvious conclusion to be drawn from the contrasting political effects in Tables 4 and 5 is that the impact of politics on gross spending is largely a function of the tax effects now netted out of the equation. Because that is so, we devote the final section of this article to exploring the mechanism underlying these politically driven tax effects in somewhat great detail. The best-fit model for net current public expenditure (Equation 5b) does not feature political factors, but, arguably, has functionalist elements. While level of economic development has no impact, recent economic growth, a possible proxy for aspects of social need, is highly significant and, once again, omitting this variable allows our direct measure of social needs to feature as a predictor of 2001 expenditure levels. Given that the path-dependent effects of programme consolidation also feature prominently in some functionalist accounts (Wilensky, 1975), it is clear that netting out the impact of taxes immediately shifts the balance away from 'politics matters' to socio-economic theo-

**Table 6** Determinants of net current private social expenditure

| | *1c* | *2c* | *3c* | *4c* | *5c* |
|---|---|---|---|---|---|
| Intercept | –9.04*** | –12.97** | –42.86 | –9.21*** | –8.30*** |
| | (3.73) | (2.16) | (.85) | (4.11) | (4.75) |
| GDP per capita | 6.38E-04*** | 7.22E-04*** | 6.11E-04*** | 5.66E-04*** | 5.32E-04*** |
| (1960–2001) | (4.28) | (3.70) | (3.87) | (4.02) | (4.14) |
| GDP growth | .21 | .51 | .17 | .25 | – |
| (1981–2001) | (.51) | (.84) | (.40) | (.67) | |
| Bourgeois Cabinet seats | .033** | .031** | .028[b] | .022 | .027** |
| (1950–2000) | (2.35) | (2.16) | (1.75) | (1.63) | (2.18) |
| Social need index 2001 | – | .84 | – | – | – |
| | | (.69) | | | |
| Temporal consolidation of the welfare state | – | – | .018 | – | – |
| | | | (.67) | | |
| Index of federalism, bicameralism and constitutional rigidity | – | – | – | .85* | .83* |
| | | | | (1.97) | (1.97) |
| N | 18 | 18 | 18 | 18 | 18 |
| Adjusted $R^2$ | .64 | .63 | .63 | .70 | .71 |

*Notes*:
[a] Unstandardized regression coefficients; t -statistics in parentheses. * $p \leq .10$; ** $p \leq .05$; *** $p \leq .01$.
[b] = level of significance is .104.

ries of welfare determination.

The picture changes even more dramatically when we turn to the driving factors of *net current private social expenditure* (see Table 6), with all the causal mechanisms adduced to account for public expenditure reversed in their effects. Instead of economic growth being the crucial economic development variable, it is the level GDP per capita averaged over the past five decades that turns out to be the most powerful predictor of the present-day volume of private spending. The countries that have been relatively affluent during the postwar decades have outspent the countries that have been relatively less affluent. Since public and private social expenditure are, at least, partial substitutes, the strong reliance of rich countries on private social spending helps explain the curvilinear effect demonstrated in Note 1. Possible explanations for the positive relationship between economic wealth and private social expenditure are that higher economic resources sustained over long periods produce a surplus which can be used to finance private benefits or, what may be another way of saying the same thing, that affluence produces and sustains a stronger middle class, favouring non-statist forms of provision. In either case, this suggests that public welfare is an 'inferior good' in the technical sense of a good with the property that, as income rises, the demand for the inferior good falls.

No less interesting in terms of the historical evolution of comparative analysis of the welfare state, the positive relationship between affluence and private welfare spending adds a further functionalist element to the account of contemporary welfare diversity. Where, for Wilensky, affluence was the main driving force of public spending on welfare, here it features as the main determinant of cross-national differences in private expenditure. However, the emergence of one functionalist component is at the expense of another. The needs element, common to most functionalist accounts, is missing here. In earlier models (see Tables 4 and 5), removing economic growth from the baseline model allowed the social need index to feature as a significant predictor of expenditure. That does not occur in the Table 6 equations, making it quite clear that, whatever substitutability there may be between private and public spending, it is not sufficient to allow private spending to serve as anything like an adequate source for the amelioration of social need.

Table 6 demonstrates other important reversals. One concerns the timing of welfare state consolidation, with welfare state laggards showing higher levels of private social expenditure than

countries launching their public programmes earlier. Similar logics to those already noted may also account for this effect, with early and prolonged affluence, arguably, being a source of the early establishment of voluntary and private forms of provision discouraging the early adoption of public programmes (see Castles, 1998). A competing (or perhaps even complementary) explanation might be that welfare state laggards are typically countries characterized by numerous institutional veto points (r =.39). Since the impact of constitutional rigidities on private spending is positive and significant at the 10 percent level (Equation 4c), it may be argued that multiple veto points tend to encourage the development of private social expenditure. As we have argued elsewhere (Obinger et al., 2005), this appears to have been a consequence of the employment of 'political bypass strategies' designed to overcome the political stalemate caused by constitutional rigidities. We may recall that a basic axiom of veto player theory is that the higher the numbers of veto players, the more likely is political deadlock (Tsebelis, 2002). Whenever an attempt to legislate public programmes fails to overcome the institutional obstacles in its path, there remains room for private solutions and/or forms of benefit provision in which the state promotes privately organized programmes through tax allowances and incentives. Hence, there are excellent reasons for assuming that constitutional rigidities have preconfigured the public–private mix in benefit provision by redirecting pressures for programme adoption away from statist channels and into private ones.

Last but by no means least, parties matter; but not in the manner generally featuring in comparative public policy analysis, with the Left favouring greater welfare state spending and their bourgeois opponents seeking to constrain expenditure profligacy. In the realm of private social spending, it is in the countries in which bourgeois parties have been strongest that expenditures have been highest and although, once again not reported separately, it is in the countries in which the Left has been strongest that spending has been least. In partial contrast to the case of net public spending, where a socio-economic account made better sense of the realities of cross-national expenditure variance than a 'politics matters' one, both politics and economic development matter a great deal in explaining private expenditure, with our best-fit model (Equation 5c) combining the classic functionalist *explanans* with two political variables to account for around 70 percent of the variance.

Adding net public and net private social expenditure and subtracting the extent of tax breaks for social purposes towards current private social benefits provides a measure mapping the scope of *net total social expenditure*. The five models featuring in Table 7 identify the factors driving expenditure in OECD countries devoted to levels of welfare provision as a whole. Our earlier analysis of gross expenditure suggested that parties mattered a great deal, with bourgeois dominance explaining lower spending and Left incumbency higher spending. Our recently completed analysis of private expenditures has shown that parties have apparently been no less influential, although the direction of their impact is here reversed, with spending higher under bourgeois auspices. The question, then, is whether we can discern partisan effects when we come to analyse net total social expenditure in Table 7. The answer is that the joint effect of summing these categories of expenditure and netting out taxation effects on both leaves us with an account of overall social expenditure effort that is predominantly socio-economic and almost entirely functionalist in character. The level of economic development over the past 50 years is positively related to net total social expenditure, while the impact of GDP growth is strongly negative in most equations. Countries that have been rich over the past five decades spend more on welfare, while countries that have been growing richer faster over the last two decades spend less. Once again, removing economic growth from these models produces evidence of a significant, although somewhat weaker, relationship with levels of need. The only non-socio-economic influence on total spending is the marginally significant impact of welfare consolidation, with countries getting into the public welfare state business early continuing to spend somewhat more than those getting into it later.

As noted in discussing earlier findings, what is most interesting in terms of the historical development of the scholarly literature in this area is the way the models reported here restore aspects of the once influential functionalist interpretation of expenditure development (see Wagner, 1911; Wilensky, 1975; Polanyi, 1978 [1944]) to centre stage. Wilensky, the most influential sociological proponent of this view, would easily have recognized an account of total net spending premised on

**Table 7** Determinants of net total social expenditure (2001)

| | *1d* | *2d* | *3d* | *4d* | *5d* |
|---|---|---|---|---|---|
| Intercept | 19.99*** | 4.55 | 173.89* | 19.98*** | 154.52* |
| | (4.12) | (.42) | (1.95) | (4.25) | (2.00) |
| GDP per capita | 6.62E-04** | 1.00E-03** | 7.88E-04** | 5.76E-04* | 8.08E-04** |
| (1960–2001) | (2.30) | (2.87) | (2.83) | (1.95) | (3.02) |
| GDP growth | –2.68*** | –1.43 | –2.51*** | –2.63*** | –2.39*** |
| (1981–2001) | (3.37) | (1.30) | (3.35) | (3.33) | (3.48) |
| Bourgeois Cabinet seats | –.0089 | –.015 | .013 | –.021 | – |
| (1950–2000) | (.33) | (.60) | (.47) | (.73) | |
| Social need index 2001 | – | 3.46 | – | – | – |
| | | (1.57) | | | |
| Temporal consolidation | – | – | –.082 | – | –.072[b] |
| of the welfare state | | | (1.73) | | (1.75) |
| Index of federalism, | – | – | – | 1.01 | |
| bicameralism and | | | | (1.11) | – |
| constitutional rigidity | | | | | |
| N | 18 | 18 | 18 | 18 | 18 |
| Adjusted $R^2$ | .61 | .64 | .65 | .61 | .67 |

*Notes*:
[a] Unstandardized regression coefficients; t-statistics in parentheses. * $p \leq .10$; ** $p \leq .05$; *** $p \leq .01$.
[b] = level of significance is .1027.

the role of economic development, the problem pressure of social need (or its partial economic growth surrogate) and programme consolidation, since such an account was essentially his own. (Although in his case, it derived from a consideration exclusively of gross public expenditure levels, whereas the models here are for total [public + private] welfare effort.) Almost certainly the reason that the determinants of total spending in 2001 resemble those of gross spending in the mid-1960s (the data point for Wilensky's research) is that the data on which his study relied largely predate the substantial change in expenditure relativities shaped by partisan forces in the 1960s and 1970s.

## Politics and redistribution

If, then, as Adema and Ladaique (2005) tell us, total net expenditure is what really matters in assessing the extent of national welfare effort, must we agree with Wilensky's mid-1970s conclusion that partisan politics adds absolutely nothing to the explanation of social spending? In our view, the answer is a decisive no. Throughout the course of our analysis, we have presented clear evidence that political parties and, to a lesser extent, political institutions play an important role in shaping the public–private mix of benefit provision, determining where both gross public and net private spending are greatest and least. While socio-economic factors may explain how much societies ultimately spend on social provision, politics remains the key to who gets what, when and with what effect in the welfare arena. In this final substantive section of our article, we seek to demonstrate that an analysis which fails to acknowledge the explanatory power of partisan politics is unable to obtain any serious intellectual purchase on the issue which, for the majority of commentators, frames their understanding of the moral purpose and, hence, the theoretical substance of the welfare state: the fact that different kinds of welfare states produce quite different outcomes in terms of poverty and inequality.

The first step in that demonstration is to show that the different categories of spending featuring in Table 1 are, indeed, associated with different outcomes. This task is undertaken in Table 8, which reports the bivariate relationships between these different categories of spending and the latest figures for the percentage of the population living below a poverty line of 50 percent of median income and for the Gini index of income inequality as reported on the Luxembourg Income Study (LIS) website (see http://www.lisproject.org). Unfortunately, the LIS database does not report figures for poverty or

**Table 8** Correlations between expenditure categories and redistributional outcomes

| *Categories* | *Poverty Rate (50% median income)* | *Gini Index of Inequality* |
|---|---|---|
| Gross public social expenditure | –.827*** | –.684*** |
| Net current public social expenditure | –.685*** | –.495* |
| Net current private social expenditure | .379 | .418 |
| Total net social expenditure | –.488* | –.281 |
| Public social expenditure taxation incidence | –.775*** | –.752*** |

*Note*: Pearson correlation coefficient. * $p \leq .10$; ** $p \leq .05$; *** $p \leq .01$.

inequality for either Japan or New Zealand, so the correlations in Table 8 are based on only 16 of the 18 cases featuring in our earlier analysis. Since the latest LIS figures on occasions predate our 2001 expenditure measures, the findings reported here would have to be considered tentative were they not so overwhelmingly strong.

In addition to examining the relationship between the expenditure categories in Table 1 and redistributional outcomes, Table 8 also seeks to assess the redistributional impact of another measure which can be derived from the Adema and Ladaique study: the difference between gross and net public spending on welfare (i.e. expenditure categories 1 and 2 in Table 1), which is equivalent to the incidence of taxes on gross public social expenditure. This measure, which is not separately identified or named in the Adema and Ladaique study, we call *public social expenditure taxation incidence*. Potentially indicative of strong political antecedents, average family of nations' values for this variable are 5.85 percent of GDP in Scandinavia, 3.82 percent in continental Western Europe and just 1.16 in the English-speaking family of nations. In light of the recent interest in the latter group of countries in the use of tax credits as a means of targeted assistance to families and the working poor, it is worth noting that, in the English-speaking countries in 2001, the average level of expenditure on tax benefits for social purposes of a kind equivalent to cash benefits was just 0.27 of a percent of GDP (calculated from Adema and Ladaique, 2005, Table Annex 3: 71) and, seemingly, therefore, hardly of a sufficient magnitude to offset tax interventions of a more conventional kind in such a way as to affect cross-national distributional outcomes.

Because the relationships reported in Table 8 are simply bivariate correlations, we cannot claim that any of these findings, however strong, constitute anything like complete accounts of the factors shaping poverty and inequality in contemporary OECD societies. However, we may note that some of the relationships reported in the table are very strong indeed and that the table provides unequivocal evidence that gross expenditure is far more closely associated with redistributive outcomes than any of the Adema and Ladaique measures of net expenditure. Just as most studies in the field have assumed, gross spending is a hugely successful predictor of poverty levels and a moderately good predictor of economic inequality. Of the net measures, the only relationship meeting conventional standards of statistical significance is that between net current public social expenditure and the poverty rate. Although, in principle, adding in the expenditure equivalent of tax breaks for social purposes equivalent to cash benefits should have the effect of making the net current public expenditure measure more redistributive in character, the relatively small magnitude of that expenditure vis-a-vis other tax effects makes it difficult to observe this impact in practice. Moreover, the inclusion of private spending weakens the relationships further because net current private spending is actually positively related to poverty and inequality, the latter relationship only just missing out on being significant at the 10 percent level. The best which can be said in redistributive terms for the total net social expenditure measure, which Adema and Ladaique propose as the best proxy for society's total welfare effort, is that it weakly predicts poverty but has no discernible impact on income inequality. Thus, the

gross expenditure measure, which the established literature correctly argues is substantially shaped by the positive influence of Left partisanship and the negative influence of its bourgeois opponents, is a strong predictor of favourable redistributive outcomes; while the measures better accounted for in functionalist or broadly socio-economic terms turn out to be negligibly, or even positively, associated with poverty and inequality.

We have included the additional measure of public social expenditure taxation incidence in our Table 8 analysis because it is this item which, by definition, makes the difference between gross and net public expenditure and which, therefore, must be, in large part, responsible for gross expenditure's stronger association with redistributive outcomes. The final row of figures in Table 8 confirms that this is so, with tax incidence, by itself, almost as good a predictor of poverty outcomes as is gross expenditure and actually a rather stronger predictor of inequality than gross spending, or indeed, any other measure featuring in Table 8. So the important story here is that what really matters about welfare state redistribution is a function of the incidence of taxation, with the simple syllogism: the greater the taxation of gross spending, the greater the welfare.

This may appear counter-intuitive if one thinks of the impact of taxation only in terms of a reduction in recipients' prior levels of well-being, but less so if one thinks in terms of a modified Robin Hood analogy. Robin Hood apocryphally stole from the rich and gave to the poor. Taxing those welfare recipients in reciept of higher benefits and with greater affluence is the stealing from the rich part – but with the greater subtleties of the modern fiscal system allowing the proceeds to be used not for the kind of crude wealth transfer which occurred in Sherwood Forest, but rather to finance more generous benefits and higher levels of gross spending. Using the tax system to provide tax credits to the poor is another recent subtlety; but, as we have seen so far, not one with any discernible impact on cross-national outcomes. Indeed, it is arguable that, as an instrument supposedly undermining the rationale for high and universal benefits, the push for tax credits may actually reduce the incentive for generous treatment to the poor. The evidence reviewed in this article suggests that it is because the countries of Scandinavia and, to a lesser extent, continental Western Europe tax a lot that they can afford to spend a lot on the higher benefits required to alleviate poverty. In turn, it is because the middle classes and the most affluent in these countries end up paying more in taxation than elsewhere that inequality is lower.[3] Economists are wont to decry the combination of high benefits and high taxation, suggesting that this phenomenon, which they call 'churning', leads to a serious misallocation of resources and hence to a reduction in economic performance. Our analysis, however, suggests that the combination of high levels of taxing and spending cannot simply be rejected on grounds of economic inefficiency, but rather represents a policy strategy deliberately chosen on partisan grounds to enhance welfare redistribution (for a confirmatory theoretical analysis, see Åberg, 1989; c.f. Korpi and Palme, 1998; Rothstein, 2001).

That it is partisan politics which sets this redistributive mechanism in motion can be inferred simply from the fact evident earlier on in our analysis that gross expenditure is strongly negatively associated with bourgeois incumbency and net public expenditure is not. Given this, it seems unnecessary to provide a further complete set of regressions reporting findings the import of which is already understood, and we content ourselves here with a footnote reporting a best-fit equation showing that the only significant predictors of public social expenditure tax incidence are bourgeois incumbency and, interestingly, although only significant at the 10 percent level, the negative impact of multiple constitutional veto points.[4] The obvious conclusion is that the Robin Hood effect – or, with the more positive valuation that the authors of this article prefer, the welfare-conferring effect – of the taxation of social expenditure is, to all intents and purposes, an exclusively political effect. How dramatic that effect is, and how little room there is for alternative explanations, is made evident by the scatterplot (Figure 1) with which we conclude our substantive analysis. This demonstrates both the strength and extraordinarily linear character of the relationship between partisan incumbency and the tax incidence variable, a relationship as strong as any ever reported in the 'politics matters' literature.

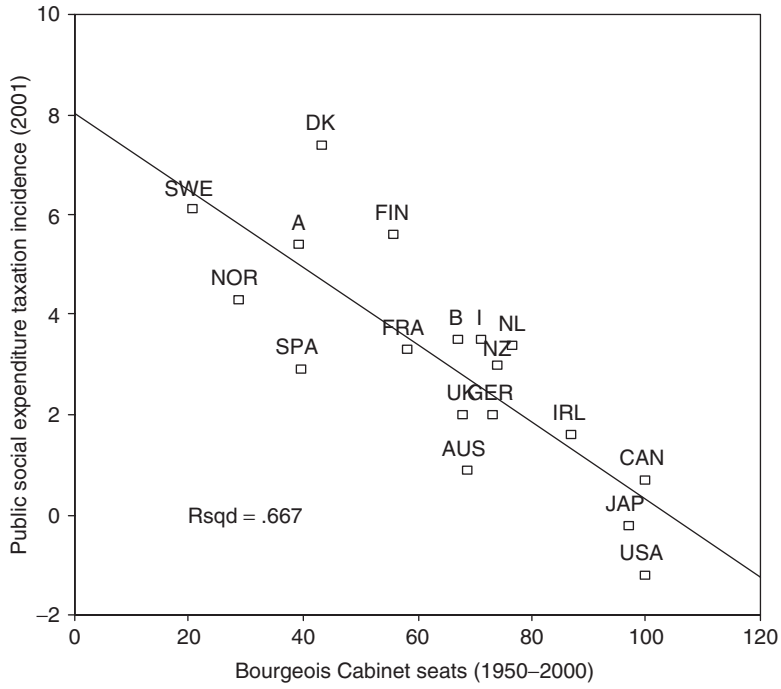


**Figure 1** The association between the partisan complexion of government and taxation incidence in 18 OECD countries

## An afterword

It is not our intention to repeat here conclusions which have already been amply stated and restated throughout the course of this article. The only point we seek to clarify in this final paragraph is our take on the original net expenditure research by Adema and Ladaique, which provides both the data and the rationale for this analysis. We have built our account of the factors shaping social expenditure around a critique of Adema and Ladaique's view that net measures of spending provide a more comprehensive account of the extent of the social support afforded by a political community than gross measures of spending. We reject that view because, as we have shown, it is gross spending – and the tax incidence which shapes it – that is central to the redistributive purposes of the welfare state and which, hence, should figure centrally as an aspect of the core indicator chosen to capture the extent of national welfare state effort.

To make it very clear, there is nothing else that we criticize or reject in this research. On the contrary, it is only Adema and Ladaique's meticulous empirical enquiry allowing us to distinguish between these multiple categories of social expenditure in so many different countries which makes it possible to locate the differential determinants of different categories of social spending and to identify the mechanisms linking party ideologies – and, to a lesser extent, political institutions – to redistributive outcomes. Moreover, if the overall lesson that governments and political and economic commentators were to draw from Adema and Ladaique's analysis is that low gross expenditure countries are often, in net terms, expending no lesser resources than ostensibly bigger spenders, but getting far less distributional bang for their buck, the study we have reviewed here might just serve as a tipping-point for the adoption of policies better attuned to the achievement of the 'theoretical substance of welfare states'.

## Appendix

**Table A1** Correlation matrix for the independent variables

| | *Adoption of social programmes* | *Bourgeois Cabinet seats* | *GDP per capita* | *Institutional veto points* | *GDP growth* |
|---|---|---|---|---|---|
| Bourgeois Cabinet seats | .553 | | | | |
| GDP per capita | .282 | .168 | | | |
| Institutional veto points | .390 | .427 | .342 | | |
| GDP growth | .227 | .373 | –.299 | .017 | |
| Social need index | –.082 | –.269 | –.310 | .040 | –.574 |

### *Notes*

1 This holds only for linear specifications of the model. Modelling a curvilinear (inverse u-shaped) effect of economic affluence on social spending yields significant results: GROSS PUBLIC EXPENDITURE 2001 = – 40.47 + 9.08E-03 GDP (2.60) –3.21E-07 GDP SQUARED (2.56); $R^2$ = .31. See Castles (2001) for an exposition of this argument.

2 Some economists might wish to object that the causal reasoning implied here is mis-specified, with low growth rates seen as being determined by high public spending levels. We do not wish to go into this debate, which has its own huge literature (for a review, see Castles and Dowrick, 1990), beyond pointing out that, for the period we are discussing and the same 18 countries featuring here, there is only a relatively weak association between gross spending in 1980 and subsequent 1981–2001 economic growth (r = –.43; sig. = .076), while there is a far greater and more significant one between growth over the same period and gross spending in 2001 (r = –.78; sig. = .000). This strongly suggests that economic growth shapes expenditure levels much more than the other way around.

3 The argument here does not deny that the incidence of taxes *within a given country* is at best likely to be proportional and may even, over some ranges of the income distribution, be regressive (social security taxes often have contribution ceilings and it is well known that the effective indirect tax rates paid by the rich are often less than those paid by the poor), but rather rests on the fact that, *in comparison with other countries*, the middle classes and the affluent in these nations pay back in taxes a greater proportion of what they receive in benefits (typically, in the English-speaking countries, no income taxes are levied on flat-rate minimum or means-tested benefits and social security contributions and indirect taxes were introduced later and are levied at lower rates than in Scandinavia and the countries of continental Western Europe).

4 The model is as follows: PUBLIC SOCIAL EXPENDITURE TAXATION INCIDENCE = 8.93 –.066 BOURGEOIS CABINET SEATS (4.72) –.890 INDEX OF FEDERALISM, BICAMERALISM AND CONSTITUTIONAL RIGIDITY (1.95). Adjusted $R^2$ =.70.

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