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## 12 To Reform or Not to Reform? Explaining the Coexistence of Successful Pension Reform and Sick Pay Inertia in Norway

### 12.1 Introduction

Why do some aspects of welfare policy lend themselves to radical reform, while others seem to resist all demands for reform and retrenchment? How can we understand that institutional change takes place to such different degrees and in such different manners in different parts of the same welfare state? Differential reform capacity in different policy areas of the welfare state is a largely unexplored area of research. Yet, there are several advantages to comparing the occurrence of institutional change in different areas of the same welfare state. One is that such within-country comparative analysis allows us to “control for” the pressures of globalization and budgetary constraints that tend to dominate much of the literature and ask questions about other and more internal drivers of change. By focusing specific programmes and reforms we are able to examine the details of interest group configurations, institutional heritages and ideological struggles that pertain to specific policy areas and specific reform processes.

In this chapter we try to explain what appears to be a puzzling difference between the contemporary dynamics of pension policy and sick pay policy in Norway. Despite persistent concerns about comparatively high sickness absence rates, the basic structure of the extremely generous Norwegian sickness insurance has remained nearly unchanged since 1978. This is all the more surprising as there have been several failed initiatives by successive governments to cut benefits and to improve the incentive structure vis-à-vis both employers and individual employees and because the case deviates from general tendencies towards retrenchment in other countries' sickness insurance systems. The story of the Norwegian pension reform is quite different. Here the Norwegian political system in 2009 delivered a fairly radical structural reform that promises to secure economic sustainability in the face of an ageing population. The successful implementation of the pension reform is surprising in its own right as it has been enacted despite *comparatively* weak reform pressures and in the absence of an acute economic crisis that might otherwise have offered reform eager politicians an opportunity for breaking popular resistance (Pierson, 1996).

In the following we first present three different theoretical perspectives which have been dominant in the literature on social policy reform processes. The first perspective views policy reform processes as the result of strategic games, emphasizing the preferences, priorities and power-resources of collective actors and stakeholders. The second perspective concentrates on institutional factors and mechanisms of path

dependency. Finally, the third perspective focuses on the significance of discourse and framing in the policy reform process. We argue that there are good reasons to combine such perspectives when analysing complex policy processes, in particular as, in practice, they are not easily separated. Institutional configurations, such as the tripartite collaboration on policy making that is crucial in the field of Norwegian sickness insurance, cannot be understood without taking into account the strategic interests of the major players, but they also give shape to a particular kind of discourse with repercussions on the scope for future policy making. After introducing the theoretical perspectives we present the two cases briefly, before we move on to comparatively analysing the cases in light of the three perspectives.

## 12.2 Theoretical Perspectives on Social Policy Reform

Power resource theory was for many years the dominant perspective in comparative welfare state research, particularly in the quantitatively oriented branch. According to Paul Pierson, this perspective “has had considerable success in accounting for cross-national variations in social provision during the three decades following World War II” (Pierson, 1996, p. 150). The essence of the power resource perspective is well captured by its leading proponent Walter Korpi (1989, p. 313): “...in the power resources perspective, political parties and other interest organizations (...) tend to appear as the organized expressions of collective action geared toward safeguarding the diverging interests of groups differently located in the social structure”. In comparative research this very general perspective was most often given a more narrow interpretation in which the conflict between labour and capital took centre stage and the mobilization of the working class through trade unions and left parties was seen as the key to welfare state expansion (Korpi, 1981).

When Paul Pierson launched his famous thesis about a New Politics of Welfare, one of the central premises was that organized labour had been seriously weakened by the late 1980s and that the apparent resilience of developed welfare states to efforts at retrenchment must be explained by other factors (Pierson, 1996). Of course Pierson’s general claim on this point has been controversial. Particularly in Scandinavia the underlying premise about a serious weakening of organized labour as a political force does not seem to fit reality. In the Norwegian case it is rather obvious that any attempt to explain reform and resilience in welfare policy needs to take account of the positions taken by the trade union movement and its strategic interaction with the employers and the political authorities.

Institutional approaches are concerned with the impact of welfare state structures and political institutions on the potential and direction of policy reform. While much early welfare state research interpreted the development of welfare state programmes as responses to functional needs or power constellations between social actors, institutionalism brought politics and the state “back in” (Skocpol, 1985).

Much institutionalist writing focuses on characteristics of the political system and examines how these can impact the extent and shape of welfare policies. In these studies elements such as the electoral system, whether there is a president or a parliamentary system and the presence of veto points such as second chambers are crucial variables, sometimes in combination with partisan variables. However, for the comparative analysis we are doing of two different branches of welfare policy within the same country, these institutional political variables are less relevant – our cases are played out within the very same political system and in much of the same time period. However, de facto veto points may be differently set up in sickness insurance and pension policy as these are also embedded within the system of tripartite relations (including negotiated wage agreements). More relevant for our purposes are the bodies of literature that focus on the welfare state institutions themselves in shaping the conditions of reform. This type of analysis has tended to focus on feedback effects and *path dependence*. More specifically, we shall here examine what Pierson (2000, 2004) refers to as the logic of *increasing returns*. While path dependency – in its broader sense – simply refers to the causal relevance of preceding events (history matters), a narrower and theoretically more powerful understanding of the concept points to mechanisms whereby policy developments after some critical turning point become locked into a particular, self-reinforcing development track. This conception of path dependence is closely related to the idea of increasing returns, suggesting that there is a cumulative effect: “In an increasing returns process, the probability of further steps along the same path increases with each move down that path” (Pierson, 2000, p. 252).

The emphasis on path dependencies naturally leads to a bias towards analyses of barriers to change, institutional inertia and stability. Against this, institutionalist scholars have more recently turned towards theorizing and studying gradual or *incremental* institutional change. Exogenous shocks may be necessary to generate radical institutional reconfigurations, but endogenous developments of institutions may still take place in more gradual and slow-moving ways. Thelen and co-authors suggest a typology of such incremental institutional change, distinguishing between displacement, layering, drift and conversion. In displacement existing rules are removed and new ones introduced. Layering involves the introduction of new rules on top of or alongside existing ones. Drift is the changed impact of existing rules due to shifts in their environment. Conversion means that rules remain formally the same, but are interpreted and enacted in new ways (Streeck & Thelen, 2005; Mahoney & Thelen, 2010). This perspective allows for greater sensitivity to the different kinds of political dynamics and actor constellations that underlie processes of change.

Another twist to institutionalist writing is made by authors such as Vivien Schmidt (2002, 2008), who has pointed to how institutional change is facilitated or barred by the discourses policy makers and politicians use to negotiate and argue for policy reform. She distinguishes between four fundamental functions performed by discourse in the policy process. The cognitive function of discourse is to define

the purposes of policy reform and the problems it is set to solve and offer policy instruments and methods appropriate to address this. The normative function of discourse involves demonstrating the policy programme's consistency with political goals and ideals, for example by appealing to national values and identities. While these two functions belong to the ideational dimension of discourse where policy proposals are framed in ways that may or may not appeal to our brains and hearts, respectively, the next two functions make up the interactive dimension of policy discourse. Of particular importance to our analysis is the coordinative function, which means that a common language (epistemic community, discourse coalition) is created whereby different actors can communicate and come to agreement on a specific policy programme. Finally, the communicative function of discourse is about how policy actors are able to communicate a policy programme to the public.

### 12.3 Case I: Sickness Insurance

The Norwegian sickness insurance scheme is often labelled “the most generous in the world”, and, currently, it probably is. It entitles employees to full wage compensation for up to a year.<sup>1</sup> The employers pay for the first 16 days, and thereafter National Insurance carries the full financial responsibility. Employees can self-certify the first three days of absence – more if their employer is part of The Agreement for a More Inclusive Working Life (*IA-avtalen*).

Remarkably, this scheme and the associated economic incentive structure have remained nearly<sup>2</sup> unchanged since its introduction in 1978. The scheme was introduced by a reform in 1977. It was pushed forward by the left and the labour movement but eventually passed in Parliament by a unanimous vote. It gave all workers access to sick pay benefits at a 100 per cent replacement rate, something which many white-collar workers had already enjoyed for years. The concerns that existed over potential abuse were trumped by arguments for equal treatment of blue- and white-collar workers. There has, in the decades since the scheme was enacted, been no shortage of demands for and attempts at retrenchment reform. At several points in time, especially when sickness absence figures have been on the rise, public commissions have been appointed to address the issue. They have pointed to problematic aspects of an economic incentive structure that, firstly, gives few incentives for employees to return

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**1** The insurance is paid out up to a maximum ceiling of six basic amounts, currently about 500 000 NOK/66 000 EURO. Many employers, including the state, also top this up so that a large share of more high earning employees also enjoys a 100 per cent replacement rate.

**2** The employer period was extended from 14 to 16 days in 1998. There have also been some minor adjustments of entry criteria, maximum ceilings and so forth, but the main principles of 100 per cent sick pay and two weeks of employer funding remain intact.

to work, and, secondly, does not induce employers to take steps to make workplace adaptations and other measures to bring sick employees back into work (NOU, 1990, 2000; Mykletunvalget, 2010). Both left-wing and right-wing governments have, typically in association with the preparation of the annual state budget, made formal proposals to extend the employer financing period and, more rarely, to introduce an element of self-risk for employees.

But resistance has been fierce, and all claims for change have ultimately failed. In the case of employer financing, a significant argument has been the fear that higher costs will make employers more reluctant to employ persons with poor health, thus excluding persons with impaired health from the labour market. With respect to sick pay cuts, it is a powerful argument that these will hit women and low-paid, low-educated employees the hardest, as these are the groups that tend to have the highest levels of sickness absence. In any case, Norwegian sickness insurance seems to provide a strong example of institutional inertia.

Instead of benefit cuts and changes in the incentive structure facing employers, a policy strategy has been pursued emphasizing tripartite collaboration (between the state and the social partners) for more efficient workplace-orientated measures against sickness absence. In 2001 conflicts over possible sick pay cuts were resolved through the establishment of the first IA-agreement. The state and the largest employers' and employees' confederations joined forces to reduce sickness absence. Workplace-orientated measures emphasizing early intervention, monitoring and dialogue between employers and employees were pursued in combination with a move away from diagnosis towards functional assessments and functional ability – in sum encouraging an approach where adaptations and cooperation in the workplace should enable people to stay at work and return to work sooner despite health problems (Hagelund 2014). The agreement rested, however, on the condition that the government would not make any further claims to change the economic incentives in the sickness insurance. Thus the social partners had effectively been set up as veto-players through tripartite negotiations, with limited public debate. Despite its failure in reaching the original target of a 20 per cent reduction in sickness absence, the IA-agreement has since been renewed twice. Furthermore, measures established in the context of IA-negotiations have also been incorporated in general law, thus applying to the entire labour market. These include increasingly detailed regulations of the steps to be taken to follow up sick listed employees through individual plans and compulsory meetings. In this sense institutional change is taking place but in an incremental manner which neither takes the shape of radical reform or affects workers' rights to sick pay. Instead layers of new rules and regulations are added on top of the existing sickness insurance. Indeed, it seems that it is this very process of *layering* that has enabled the state and the social partners to establish a new consensus about protecting sickness insurance from retrenchment.

## 12.4 Case II: Pension Reform

The existing Norwegian old-age pension system is less spectacular from a comparative perspective. The main features of the old “National Insurance” system date back to the late 1960s when a two-tier system of public pension provision was introduced combining an existing universal flat-rate benefit with an ambitious new earnings-related second tier. While the reform was eventually adopted with broad parliamentary support, the original impetus came from organized labour. The Norwegian LO (the Norwegian confederation of trade unions) had since the late 1950s demanded improved income protection for blue-collar workers and a levelling of pension rights with white-collar workers and civil servants who were covered by voluntary, employer-financed pension schemes (Pedersen 1990; Hippe & Pedersen, 1996). The introduction of an earnings-related second tier was believed to make additional occupational pension coverage redundant, but as it turned out supplementary occupational pension schemes continued to play an important role, particularly for employees in the public sector.

Concerns about the long-term fiscal sustainability of the National Insurance system had already begun to surface in the early 1980s. A process of policy deliberation initiated by a centre-right government but later taken over by a Labour government resulted in the enactment in 1989 of a smaller parametric reform that involved modest cuts to future replacement rates. As a consequence the importance of supplementary occupational pension schemes grew even more.

In the 1990s opportunities for early retirement were expanded. In 1988, at the onset of an economic downturn, the LO managed to persuade the employers association (NHO) and the Labour government to establish a contractual early retirement scheme (the so-called AFP-scheme) that allowed employees covered by a collective wage agreement to retire before the normal retirement age of 67 without any actuarial penalty. In the following years the early retirement age in the AFP scheme was lowered in several steps to reach 62 years in 1997. The gradual expansion of this scheme, which heavily subsidized early retirement, was reluctantly supported by successive governments, but concerns were growing among policy analysts and the political elite – including the leadership of the Labour Party – about declining effective retirement ages.

The current pension reform process started when a Labour minority government in 2001 appointed the so-called Pension Commission with a mandate to investigate the need for a major reform of the entire system of income protection in retirement. The Commission included prominent representatives from each of the parliamentary parties as well as a number of independent experts. Contrary to standard practice, the social partners were not directly represented in the Commission and were only invited to join an adjacent consultative body.

The Commission published its report in early 2004 (NOU, 2004, p. 1). It contained a majority proposal for a comprehensive structural reform of the National Insurance

pension system. In the following years the reform was carried through the political system by shifting governments with only small modifications. It was finally enacted in 2009 by a broad coalition of parties - excluding only the populist right party (the Progress Party) – and the reform took effect from 1 January 2011.

The content of the reform is strongly inspired by the innovative Swedish (and Italian) pension reforms from the previous decade. In the new system the accrual of old-age pension rights will follow the Notional Defined Contribution (NDC) formula. However, despite the transition from a traditionally defined benefit to a defined contribution formula for the accrual of pension rights, the overall distributive profile of the new system is not all that different from the old system, as both the ceiling on yearly earnings and the Guarantee Pension help maintain a fairly progressive overall benefit profile (Christensen, Fredriksen, Lien & Stølen, 2012).

In addition, the reform introduced a flexible retirement age between 62 and 75 years on actuarially neutral terms, which means that the new system provides very strong incentives to postpone retirement. In the national wage negotiations in 2008 the government managed to persuade the social partners in the private sector to transform the existing private AFP-scheme so that it also conforms to the principle of actuarial neutrality, and, hence, in the private sector all subsidies for early retirement have been effectively removed.

The reform contains two retrenchment measures of which the first – life expectancy adjustment – is the most important. Old-age benefits will in the future be reduced in proportion to observed increases in longevity. It is estimated that the life expectancy adjustment will result in a 20 per cent reduction of pension benefits for the cohorts retiring around 2050. Thanks to the flexible retirement age, however, pensioners can in principle compensate for the reduction in yearly benefits by postponing retirement and working longer. The other retrenchment measure concerns the indexation of pension benefits that are no longer supposed to take full part in general real wage increases. It is estimated that this measure will achieve a reduction in pension expenditures of about 7 per cent compared to full wage indexation. It is projected that the reform will result in a reduction in projected pension expenditure in 2050 from 15 to 12 per cent of GDP.

The Norwegian pension reform is remarkable because it has been carried through despite rather modest reform pressures. Public expenditure on old-age pensions is currently relatively low due to a combination of moderate benefit levels and a comparatively high effective retirement age, and the Norwegian state is in an extremely fortunate situation with yearly surpluses on the budget in the area of 15 per cent of GDP that are set aside in a state-owned provident fund – known as the Norwegian Petroleum fund (renamed the Government Pension Fund Global in 2006) – and invested in international capital markets.

However, a major setback in the pension reform process happened in 2009 when the government failed to persuade the public sector unions to accept a reform of the public sector version of the AFP-scheme and the public sector occupational pension

schemes. This means that two main principles of overall reform – transition to an NDC-formula with lifelong accrual of pension rights and a neutral system for drawing benefits – have not been implemented in the public sector, which in Norway accounts for roughly one-third of the workforce.

## 12.5 Actor Constellations and Strategic Games

Power mobilization theory and a rational choice perspective on policy making would lead us to believe that organized labour and the Norwegian LO in particular would be strongly opposed to retrenchment reforms in both sickness benefits and old-age pensions. As we have seen, in both areas the existing welfare arrangements have come about as a result of political processes in which the LO was heavily involved – in the 1960s and the 1970s, respectively. In fact, both the existing sickness benefit system and the public pension system can be viewed as the realization of historical claims made by the LO on behalf of its constituency of wage earners.

How can we explain, from a rational power-resource perspective, the fact that the LO has succeeded to insulate the sickness benefit scheme from all attempts at cut backs, while it on the other hand has been forced to accept an ambitious structural pension reform?

Clearly a general weakening of organized labour as a political force, that Pierson seemed to take for granted in the original formulation of his New Politics of welfare thesis (Pierson, 1996), would not account for the differential outcome, and this diagnosis simply does not fit the Norwegian case. In the 1990s tripartite cooperation was strengthened in Norway, and successive governments depended heavily on cooperation from the LO to deliver the necessary wage restraint to help secure competitiveness and macro-economic stability (Dølvik & Stokke, 1998). The introduction of the early retirement scheme (AFP) and its expansion over the 1990s is a clear indication of the substantial bargaining power of the LO vis-à-vis the employers association (NHO) and successive governments.

We therefore need to take into consideration 1) the priorities that the LO has given to defend its preferred position on the different issues (sickness benefits and pensions) and 2) the strength of interests and the power resources that other important actors have brought into the process.

It is apparent that the LO has signalled a strong sense of ownership of the sickness benefit programme and hence a strong commitment to defend it at all costs, while the LO appears to accept not to have a de facto veto-power over any changes in the public pension system. This differential approach to the two policy areas can be viewed as a rational prioritization and adaptation to the fact that the set of stakeholders and institutional context for reform in the two fields differ. In the sickness benefit case the LO deals with only two other main actors, the employers' association (NHO) and the government, while the pension policy field involves a much larger set of actors

and interests such as the pension industry, the women's rights movement, the self-employed, consumer and pensioner organizations, etc. Furthermore, all parts of the LO share an interest in maintaining generous sick pay. With respect to pensions, there are important internal divides that must be managed and contained, particularly between private and public sector workers, but also between male and female workers and younger and older cohorts. Finally, the policy alternatives for sickness insurance reform appear to be relatively simple compared to the complexity of pensions reform. In both cases however, the LO has been willing to accept compromises that promise to fend off less desirable alternatives.

The absence of a sickness insurance reform can be explained as the result of a strategic game, where the three actors had different preferences concerning the ranking of four alternative policy outcomes. In 2000/2001, when the conflict over sickness insurance reform was at its height, there were four available policy alternatives: A. to maintain status quo – no changes in the economic incentive structure and continued tripartite cooperation through the IA-agreement; B. increased employer financing; C. reduced sick pay; D. a combination of increased employer financing and reduced sick pay.

There is strong disagreement about the ranking of these alternatives between the three actors. The LO gives top priority to maintaining status quo but could probably also accept increased employer funding. The employers' association (NHO) would ideally prefer one-sided cuts in sickness benefits, but it is not as strongly concerned with rolling back the sickness benefit scheme as one might assume (see Swenson, 2002). What the NHO fears the most are one-sided increases in the degree of self-insurance required by employers, and hence the NHO actually prefers the status quo where the state takes the bill of sickness absence over a solution where the costs are put more heavily on employers. The NHO has however signalled that it is prepared to accept a combination of moderately increased employer funding and sick pay cuts. The latter also appears to have been successive governments' preference, following recommendations made by a government appointed committee in 2000 (NOU, 2000, p. 27). So why has an alliance between the government and the employers' association not been forged in an effort to overcome LO's resistance? For both successive governments and for the NHO a head-on confrontation with the LO on this issue might not be worth the cost of jeopardizing the successful tripartite collaboration to maintain wage-constraint that helped to bring Norway out of the economic downturn of the early 1990s. For successive Labour Party governments this line of action would also involve high tactical risks. Welfare cutbacks made in alliance with the employers' association against the will of the labour unions would threaten the Labour Party's credibility on welfare issues. For the NHO a potential danger associated with a retrenchment of sickness benefit rights would be that it opens up the field for a radical increase in employer responsibilities on the financing side.

Finally, one could ask why successive Labour governments have not introduced employer co-financing of sickness benefits against the will of the NHO. Such a move

would presumably not be strongly against the interests of the LO and other labour organizations, but on this issue the LO has committed itself to take sides with the NHO in defence of the status quo. We have, in other words, a situation where the LO and the NHO have formed a tactical alliance to maintain the status quo and against any attempts by the state to give either employees or employers increased burdens. This protects them both from the less desirable alternatives of one-sided cuts that in the next round could be used as ammunition for further cuts in the other direction.

Taken together, maintaining the existing incentive structures but incorporating this into the Inclusive Working Life framework can simply have turned out as the best alternative that was possible without breaking with the corporatist model of macro-economic steering that has dominated Norwegian policy making for decades.

In the field of pensions, the LO apparently has a weaker sense of ownership of the existing system. Part of the explanation is historical. The National Insurance system was introduced in 1967 with broad political support, and although the most important political initiative had been taken by a Labour government in 1963, the final legislation was carried through parliament by a non-socialist government that came to power in 1965. More importantly, interests and policy preferences are more complex, and more actors are involved in the pension field. Also differences in interests between public and private sector employees add to the complexity of the issue and make it difficult for the LO to follow a clear-cut strategy of defending the status quo.

While the LO accepts being among a group of actors with a legitimate stake in the National Insurance scheme, its sense of ownership of the contractual AFP-scheme was and still is very strong indeed. When LO in the 1990s accepted parametric cutbacks in the public pension system, the organization gave high priority to an expansion of the possibilities for early retirement in the form of the negotiated AFP-scheme.

The expansion of the AFP-scheme and an associated decline in effective retirement age during the 1990s was eventually considered a serious long-term threat to the national economy by experts and the party political elite, and in the late 1990s tensions were building up between the LO and the Labour party leadership over the AFP scheme and its effect on the labour supply of older workers. The ambition of the Labour Party leadership to find ways to reverse a threatening lowering of the effective retirement ages was probably among the most important motives for the appointment of the Pension Commission in 2001. The Labour government wanted to avoid a head-on confrontation with the LO that would have been the result of an isolated and direct attempt to roll-back the AFP-scheme. Instead it launched a more general pension reform process involving all the other political parties – a process where a curtailment of subsidized early retirement would be only one of many themes. Our interpretation is that the Labour Party leadership tried to form a policy cartel with the other mainstream political parties in an attempt to overcome reform resistance from organized labour and the LO in particular (Weaver 2006).

When the report from the Pension Commission was published in 2004 the Labour Party leadership (at the time in opposition) decided to change strategy and seek a

compromise that would induce the LO to support the reform. In the spring of 2005 the Labour Party leadership managed to receive official backing from the LO to pursue a compromise over the pension reform with the non-socialist parties. One of the concessions to the LO that was accepted by the Labour Party leadership and taken into a political agreement with the other political parties was that the AFP scheme should be maintained, although with stronger incentives to postpone retirement. In the private sector wage negotiations in the spring of 2008 it turned out that the red-green government that had come into power in the autumn of 2005 insisted on achieving a neutral system of claiming pensions and a complete removal of all subsidies for early retirement. After tough negotiations the government succeeded in achieving this despite strong scepticism among trade unions. This result cannot be seen as anything but a defeat of the primary policy preference of the LO. The breakthrough must, however, be seen in light of the fact that it came in a period with a very tight labour market where the possibilities for older workers to extend their career appeared to be extremely good, and hence many rank and file LO members saw their interests served by a more flexible and neutral system for claiming old-age benefits. In other words, the timing of the political bargaining process in relation to the business cycle was arguably of great importance and a good example of the importance of sequencing and conjunctural causation in time (Pierson, 2004). An appealing feature of the new system – in particular in periods with abundant work for older workers – was the abolition of the work-test and the associated possibility to start claiming your pension while continuing in full-time work. The reform was also accompanied with heavy side-payments to the LO in the form of a guarantee to maintain the state subsidies to a transformed (actuarially neutral) AFP-scheme and promises to soften the implementation of the life expectancy adjustment for older cohorts.

The impressive success of the red-green government in the private sector negotiations in 2008 was followed by a rather spectacular defeat the following year as it failed to achieve an equivalent breakthrough in negotiations with the public sector unions (only some of which are affiliated with the LO). There are a number of candidates for explaining this differential outcome. One is that public sector unions had a stronger bargaining position due to stronger legal protection of their existing occupational pension schemes. In addition important public sector unions outside the LO have proved to be more uncompromising in their defence of the status quo. Finally, the timing was not beneficial. The advent of the financial crisis tended to make the employment prospects of older workers less bright than they had been a year earlier, and an upcoming parliamentary election in 2009 made a flat-out conflict with the public sector unions an unattractive alternative for the government. The government did however manage to implement one crucial component of the reform also with respect to employees in the public sector. The life expectancy adjustment factor will – at least in the long run – be implemented with equal force also in public sector occupational pensions.

Finally it is possible to speculate that there is a direct causal relationship between the differential outcome in the two policy areas: The dedication of the LO to an uncompromising defence of the sickness benefit programme made it necessary for the organization to be more compromising in the area of pensions. To simultaneously defend both against the primary policy preferences of the ruling Labour government (supported by an even more reform-eager non-socialist opposition) might simply have been perceived as impossible or, at least, too politically costly for the LO-leadership. A similar argument can be made for the Labour governments involved. A reform of the pension system (against the primary preference of the LO) was deemed more important than a curtailment of the sickness benefit programme, and hence the former was chosen at the expense of the latter.

## 12.6 Institutional Dynamics and Path Dependency

The idea of path dependency implies that once a specific policy path has been chosen, further steps will tend to move in the same direction. An external shock will often be necessary to instigate more radical changes. From this perspective the situation in 1978, when the new universal sickness insurance came into effect, constituted a formative moment with repercussions for decades to come. Relatively protected from external shocks in the sense of deep recession or mass unemployment, the system has been hard to change. What has once been given as a right, tends to be conceived of as precisely that, given rights as in not to be touched. But in view of this, how was the pension reform possible? Is the logic of path dependency played out differently for the two cases?

One crucial difference between the two systems is their levels of complexity. The pension system is complicated. Most people are uncertain about the precise content of their rights. Rights differ vastly between individuals depending on their wages, work hours, length of careers and so forth, and public pensions are complemented by a plethora of collective and private agreements. Compared to this, sickness insurance is an incredibly simple and comprehensible system. You earn full rights after only a few weeks of employment, and the deal is both generous and easy to understand – full wages during sickness. There may even be an element of 100-per-cent-magic at play: It can appear more dramatic to change something from 100 per cent to 98 than from 90 to 80.

On the other hand, there are elements about the sickness insurance design that one could expect would make it easier to change. As noted above, in an increasing-returns situation – Pierson's stricter conception of path dependency – the costs of changing paths increase over time. Every step taken down the same track *increases* the chance of the next step going in the same direction. This can for example be due to large set-up costs or learning effects that makes change expensive. Extending the employer financing period or reducing sick pay are for most practical purposes rather

simple changes that entail small costs and potentially large gains for the authorities. Indeed, this is one reason that several governments have suggested such changes as a means to bring the budget into balance. Also, unlike old-age pension, citizens have not built up their rights to sickness benefits over time, thus no complicated transitional arrangements would have to be made as has been the case in the pension reform process.

The costs of changing paths in the case of sickness insurance are probably of a political rather than a practical or financial kind. Especially through the IA-agreements all the parties have invested heavily into building positive collaborative relations. The political costs of exiting the agreement would be more dramatic now, after 14 years, than it would have been in 2003 when the question of whether to continue the agreement was first raised. Interestingly, Pierson also makes an argument about how the increasing returns-logic works through ideological factors: "Once established, basic outlooks on politics, ranging from ideologies to understandings of particular aspects of governments or orientations toward political groups or parties, are generally tenacious. They are path dependent" (Pierson, 2000, p. 260). Over time the party political consensus over the IA-agreement has broadened, and a more profound belief in this type of measure is being expressed both from the left and the right. Paradoxically then, the layering of new measures on top of the original insurance that was instigated when attempts to change the economic incentive structures failed may have made such reform even harder to accomplish in the future.

In the decades after the path-breaking reform in 1967 the pension system has been subject to incremental changes involving both drift and layering that have made the contemporary structural reform easier to accomplish. Due to a systematic under-indexation of key parameters in the system, replacement rates never reached the original target, and this has in turn allowed occupational pension schemes to play an increasing role in the overall pension system. Up until the 1990s the LO remained faithful to the ideal behind the 1967 reform of letting the pension needs of wage earners be catered to by the National Insurance scheme, and the organization looked upon occupational pension schemes with deep scepticism (Hippe & Pedersen, 1996). After the parametric retrenchment reform in the early 1990s it became apparent that occupational pension schemes were indeed needed to achieve acceptable replacement rates for wage earners with average wages, and LO unions in the private sector started to lobby for preferential tax treatment of defined contribution occupational pension schemes as a means to achieve a higher coverage among private sector workers (Pedersen, 2000). Unions in the public sector (inside and outside the LO) were opposed to the granting of tax-privileges to (employer friendly) defined contribution schemes because they feared that this could in the long run endanger the traditional, very generously defined contribution schemes for public sector employees.

When the contemporary pension reform process started in 2001, the LO was struggling with deep conflicts of interests primarily between public and private sector

unions, and there can be no doubt that this has made it more difficult for the LO to develop and carry out a consistent strategy to defend the existing pension system against retrenchment reform. This divide between the private and the public sector became evident in 2008 and 2009 when the follow-up negotiations to adjust the AFP-scheme and occupational pension schemes resulted in radically different outcomes in the private and the public sectors.

In the sickness benefit case, there is no similar divide between the public and private sectors for the simple reason that the 1978 reform was so radical as to give employees in both sectors the same right to full compensation from the first day of absence. The potential dividing effect of differences in supplementary occupational benefit systems in the two sectors was effectively removed. This is an example of increasing returns logic which also affects the actors' power resources since a higher level of generosity in sickness benefits compared to pensions creates institutional conditions that facilitate the formation of a united employee front against eventual benefit cutbacks.

## 12.7 Discourse and Framing

Discourse and framing perspectives on policy reform stress the significance of how the need for reform is formulated and communicated in order to enable actual reform. Considering the many attempts that have been made, especially to increase employer funding, it is tempting to conclude that the need to reform has not been communicated very convincingly in the case of sickness insurance, while the need for pension reform seems to have been formulated in a more compelling manner.

Vivien Schmidt (2002) suggests that such reform proposals need to attend to both the cognitive and normative aspects of discourse. Cognitive functions refer to the discourse's efficiency in demonstrating that the proposed policy will appropriately solve relevant problems, while normative functions include demonstrating the proposal's consistency with established values.

When Norwegian governments have made proposals to reform the sickness insurance, this has often happened in the context of budgetary negotiations. Thus the need for reform has tended to be framed in terms of cutting costs and securing budgetary balance. One hypothesis may be that this constitutes a narrow cognitive type of communication, which fails to appeal to core values. One infamous example stems from 2006 when the centre-left government, represented by the Minister of Labour Bjarne Håkon Hanssen, proposed to extend the level of employer funding by making employers partially responsible for the financing of sick pay also after the first 16 days. The proposal was a result of budgetary negotiations between the coalition partners, and parts of the argumentation were about freeing funds for other good purposes: "The government has ambitions to increase funding for culture, hospitals, to young families and to road maintenance. But the practical reality for government

and parliament is that the bill that needs to be picked up first is the costs of a rising sickness absence” (Hanssen, 2006). The attempt failed – rather spectacularly – when the employees’ and employers’ associations joined forces to fight what was perceived as a breach of the IA-agreement. It was quite noteworthy then when the Prime Minister three years later – again in the context of growing sickness absence – carefully suggested in a speech at an LO conference that new regulations of sickness absence again had to be considered: “It [sickness absence] is a serious problem. Both for the absentee, for the specific workplace which loses competence and for the community which is losing productive labour force and income and on which costs are incurred” (Stoltenberg, 2009). Here he is carefully constructing a problem which goes beyond the fiscal aspects of sickness insurance, appealing to crucial values of work and participation. The expert commission which was subsequently appointed to come up with new measures continued this kind of discourse, but its proposal of a restructured employer funding (paying less for shorter absences, more for longer full time absences) was also shelved. Thus, as proposals to extend or restructure employer funding (not to mention cuts in sick pay) tend to be dropped irrespectively of how crudely or cleverly they are framed, the ideational framing of reform proposals seems to have had limited impact.

However, Schmidt (2008) also speaks of a policy discourse’s interactive dimension, which consists of a coordinative function, providing policy actors with a common language and ideational framework, and a communicative function directed at convincing the public. Through the IA-negotiations, various collaborative forums and the subsequent transfusion of IA-style measures through parliament and into the general legal framework, a very strong *coordinative* discourse has emerged. The discourse of workplace-oriented measures with its stress on collaboration and dialogue in the workplace, functional ability and mobilization of remaining work capacity through adaptation of work and part-time sick leave, has succeeded in providing all central policy actors with a common language that allows for consensus solutions. However, the success of this language seems to rely on the maintenance of a fragile state of equilibrium which any alteration of the basic economic incentive structures threatens to break.

The Pension Commission clearly had an important function of fostering consensus among the political parties about the need for a reform that would limit the growth of pension expenditure in view of lower fertility rates and rapidly increasing longevity. The fact that the social partners did not participate in the Commission implied however that this consensus did not automatically extend to the trade unions and in particular not to their rank and file members. The Commission had published a preliminary report in 2002 that was meant to prepare the public for the eventual reform proposals (Pensjonskommissjonen, 2002). In both this preliminary report and the final report from the Commission, the economic and demographic challenges to the pension system were vividly presented (Ervik & Skogedal, 2014). Among the measures used to illustrate the need for reform were

calculations of the dependency ratio showing that the number of economically active per old-age pensioner would decline very significantly over the coming decades. Similarly calculations were presented to show how the necessary pension contribution of wage earners (assuming that the pay-as-you go pension expenditure should be financed entirely by wage contributions) would more than double in three decades in the absence of a pension reform. Finally, the report emphasized a comparative perspective. It showed that although Norway was currently a relative low-spender on old-age pensions, this would change in the absence of reform, and in particular it was argued that Norway would be the country in the OECD with the highest growth in pension expenditure (measured relative to GDP) over the period from 2000 to 2050 (*ibid.*).

However, the reform was not only portrayed as being necessary for financial reasons. In the reports from the Pension Commission a strong critique was raised against the existing system on justice grounds, thus also mobilizing the normative function of reform discourse. It was, for instance, pointed out how the system for accrual of pension rights, which required 40 years of contribution to receive a full pension and based the calculation of benefits on the 20 ‘best’ income years, had some rather perverse distributive effects by rewarding individuals with varying income levels over the life cycle and simultaneously punishing individuals with a more even distribution of income over the life cycle (a typical situation for manual workers).

Later in the reform process and in particular in the period leading up to the crucial negotiations in 2008 about the fate of the AFP scheme in the private sector, the reform was offensively marketed as expanding freedom of choice and as welfare enhancing by allowing older workers to start drawing their pension rights without any work-test.

It has been argued by Brooks and Weaver (2006), among others, that one of the political advantages of a structural over a parametric reform, and in particular of a transition to a NDC logic of pension accrual, is that it helps direct attention away from the retrenchment aspect of the reform and makes it difficult for the public to detect who are the most serious losers of the reform. In the Norwegian pension reform this aspect has been less pronounced because the decision to opt for the NDC formula was taken in the last minute before the publication of the Commission’s report and as the report offered rather detailed analyses of the distributive consequences of the reform.

However, the pension reform process offers some rather outright examples of obfuscation (Pierson, 1996). The most prominent is the Labour government’s promise to safeguard the AFP-scheme while subsequently insisting that the scheme should be fundamentally transformed from an early retirement scheme to become an addition to the pension wealth of affiliated workers that can be drawn on actuarially neutral terms.

## 12.8 Conclusion

In this chapter we have searched for explanations for the apparent paradox posed by the successful implementation of a structural pension reform and the persistent failure to reform sickness insurance in Norway. Three theoretical perspectives from the literature on welfare state reform have been invoked, and they all appear to contribute to an explanation.

Table 1 summarizes the three perspectives, each in two key points, and briefly outlines the situation for each of the two cases. The first perspective is concerned with the relevant actor constellations and the strategic games involved in each of the reform processes. A critical dimension is the part played by organized labour, in particular the LO. On the issue of sickness insurance the LO has acted with a high degree of unity and with a strong commitment to defend the status quo. Pension reform has been a more complicated issue for the organization, particularly as there are latent conflicting interests between the large public and private sector unions. The other key dimension concerns the alliances and compromises made in order to safeguard vital interests for the LO. Protection of sickness insurance has been ensured through an alliance with the employers' confederation, the NHO. With the more complex issue of pension reform, the LO had to prioritize its resources into safeguarding certain elements, in particular the AFP-scheme, an objective that was pursued by forming an alliance with the Labour Party where the LO had to accept other key elements of the pension reform. In the end, however, also regarding the highly prioritized goal of preserving the AFP-scheme, the LO had to concede to a solution, at least in the private sector, that was strongly at odds with its primary preference for maintaining a subsidized early retirement option from age 62. What it got instead was a preservation of the AFP-scheme in name and in terms of public financial support but a scheme that now fully complies with the principle of actuarial neutrality. This is a clear-cut example of institutional change through conversion, but as a discrete rather than a gradual process (Streeck & Thelen, 2005). Finally, it cannot be ruled out that the different positions taken by the LO in the two policy domains are directly interlinked. The battles over sickness insurance and pension reform took place simultaneously, and the LO leadership might well have decided that the political costs of going strongly against the red-green government on both issues would have been too large.

The second perspective was institutional theory, where we examined the significance of veto points and path dependencies. Again, in both reform processes the social partners in practice control vital veto points. In sickness insurance the establishment of such a veto point (in the shape of the IA-agreement) has been part of the policy compromise agreed upon. As such, the political repercussions of the IA-agreement from 2001 have been strong. A process of layering has taken place that in practice may make reform even harder to achieve in the future. In pension policy de facto veto points where the social partners effectively may neutralize at least parts of the pension reform exist – but only through the negotiations over occupational

**Table 12.1:** A summary of the key variables in a multi-perspective analysis of two policy reform cases

	<b>Power resource perspectives</b>		<b>Institutional perspectives</b>		<b>Discursive perspectives</b>	
	Degree of unity and dedication among the alliances labour unions	The emergence of	Path dependencies	Veto points	Efficient framing	Coordinative discourse
<b>Pension reform</b>	Divided interests within the LO	The LO compromises with the Labour Party in an attempt to safeguard the AFP-scheme	The system is complicated to reform; Need for complex transitional arrangements; Also complicated to adjust adjacent institutional structures (occupational pensions, disability pension) in a consistent manner	To some extent when negotiated rights are at stake. But these are multiple and decentralized, and thus potentially working in different directions.	Convincing problem formulation; Complexity which allows for obfuscation of retrenchment	Between the political parties, but excluding the social partners
Reason to expect reform	X	X		X	X	
<b>Sickness insurance reform</b>	A unified and dedicated LO against reform	The LO and the NHO form an alliance to uphold the status quo.	Fairly easy system to reform in practical terms; (But political costs may be high in terms of breaking down trust and relations established through the tripartite IA-agreement)	The IA-agreement is a de facto veto point for future reform.	Initially not very convincing, but more elaborate problem formulations have emerged; Still difficult to obfuscate the element of retrenchment	Yes, but only within the framework of the IA-agreement. Thus effectively a coordinative discourse for non-reform
Reason to expect reform			(X)			

pension schemes. The government's failure in persuading the public sector unions to accept reform of the occupational schemes means that central aspects of the pension reform are not implemented in the public sector. On the other hand, as these veto points are multiple and decentralized, it is also possible to play the various elements against each other, as when some public sector unions start to question whether they are also losing out on some of the up-sides of the pension reform – that is, the possibility to counter the effect of the life expectancy adjustment by working longer. The problem for the public sector unions is that they have forgone the opportunity to trade in their veto power over aspects of the occupational pension system for concessions concerning the content of the general pension reform. It is not unlikely that the public sector unions will eventually be forced back to the negotiating table as the life expectancy adjustment starts to take its toll, and when that happens their bargaining power is likely to be low.

Finally we looked at how the reforms have been communicated. The pension reform was presented rather convincingly – first with reference to the future sustainability of the welfare state and later as a fairness enhancing and even welfare enhancing reform. In contrast, many attempts at reforming sickness insurance have been made more hastily in the budget process with the simple purpose of saving money. Over time, however, more elaborate formulations of the need for reform have evolved, but so far with little impact in terms of policy reform. Pension policy has also offered more ample room for creative framing and persuasion (and obfuscation) compared to the sickness benefit policy where retrenchment is more difficult to hide.

The other aspect of the discourse perspective is whether an efficient coordinative discourse – a shared language in which to find policy solutions and compromises – emerges. For sickness insurance such a strong coordinative discourse has certainly evolved around the IA-agreement, but this has been a discourse entirely focused on other types of policy change than those affecting the economic incentive structure. The communicative discourse has in reality been a discourse about the need for layering in the shape of more intense follow-up procedures and activation of sick-listed employees. The Pension Commission succeeded in bringing about a coordinative discourse among the political parties on the need for reform (in the end only the Progress Party voted against the pension reform when the final bill was passed in 2009), but this consensus building did not comprise the trade unions since the social partners were excluded from participating in the Commission. This could have been detrimental to the reform process but was mitigated by the LO's willingness to seek compromises to safeguard its most treasured interests, such as the AFP. In the communicative discourse less emphasis has been put on persuading the general public about the necessity of retrenchment and about the justification for underlying principles like the life expectancy adjustment, while more emphasis has been put on selling the reform as being in some respects welfare enhancing and in others relatively harmless (Ervik & Skogedal, forthcoming).

Looking at all these dimensions in combination, the contrast between the institutional inertia of sickness insurance and the path-breaking pension reform of the 2000s – a period when Norway has been characterized by economic prosperity, low unemployment and the absence of external shocks – appears less paradoxical than at first sight. A unified and dedicated LO, the alliance between the social partners, the IA-agreement as a de facto veto point and a coordinating discourse against reform constitute solid barriers towards institutional change. While the complexity of the pension system makes it more difficult to reform than sickness insurance in purely technical terms, the complexity also works in the opposite direction by creating more contradictory actor and interest constellations, as well as allowing for a discourse where the retrenchment aspects of the reform could more easily be disguised as something else.

This chapter illustrates the interconnectedness of different explanatory variables, as well as the need to study the respective explanatory variables contextually. The strength of labour in the Norwegian context is undoubtedly an important part of the explanation for the resilience of the generous sickness insurance. But this strength is closely entangled with institutional arrangements inherited from the past that gives the different segments of the labour force shared interests with respect to defending it. The more complex pension system where the public pension system is combined with sector- and company-specific occupational schemes configures the interests of organized labour in a rather different manner and thus also rendered its voice(s) less decisive.

In his famous article on “The new politics of the welfare state”, Paul Pierson (1996) painted a rather pessimistic picture of the ability of democratic polities to adjust mature welfare systems to looming demographic and economic challenges. If such reforms were ever to be implemented, it would require that responsible politicians be able to “diffuse” the responsibility (so that voters have nowhere to go with their dissatisfaction), “compensate” powerful interest groups, and “obfuscate” the real retrenchment involved. The sick pay controversies confirm Pierson’s predictions, while the Norwegian pension reform appears to refute his pessimistic diagnosis by showing clear evidence of a significant reform capacity within the Norwegian political system. However, it cannot be denied that the three mechanisms mentioned by Pierson have all been in use at different stages in the pension reform process.

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