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Challenges of and solutions for financing long-term care

Summary

The Future of Long-term Care research stream

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Long-term care is for people who require assistance for coping with and participating in their daily lives arising from a decrease in their physical and mental capacity due to ageing or health reasons. Long-term care encompasses various healthcare and social services that prevent the deterioration of the health and abilities of people and assist them in their daily activities and wellbeing.

In OECD member countries and EU member states, the majority of the expenses on long-term care are covered from social protection financed by general budgetary income or from social security contributions. The significant contribution of the public sector upon financing long-term care arises from the high cost of care for individuals, the difficulty of anticipating the need for care, as well as the need to divide financing between generations and on the intra-generational level. Based on the aforesaid, it would not be efficient or possible for all people to separately collect savings in order to pay for expensive long-term care services, whereas it is possible to collectively ensure a more efficient use of resources and wider access to care.

The Estonian social security system as a whole is characterised by a low level of financing compared to other EU member states – while the EU average for contributing to social security is approximately 28% of GDP, the percentage stands at nearly 16% in Estonia. Likewise, the tax burden in Estonia as a whole is lower than that of the EU member states, but comparable to the average of OECD member countries. Even after a potential increase in the expenses on long-term care, we would still rank among countries with low social security expenses.

Approximately 0.7% of the GDP is used for long-term care in Estonia. This comprises 0.4% of the GDP from public sector spending and 0.3% of GDP from people's own funds. Compared to other OECD member countries and EU member states, our spending on long-term care is lower by nearly a half. While nearly 80% of expenses on long-term care are covered from shared public resources in the European Union, the respective percentage only amounts to 60% in Estonia. Increasing Estonian public sector spending on long-term care would improve the accessibility, volume and quality

of long-term care and ensure caregivers a better balance between caregiving and working.

An ageing population and the burden of caregiving for close relatives will drive the increase in the expenses on long-term care incurred by the Estonian public sector in the coming decades. The European Commission forecasts that Estonian public sector spending on long-term care will increase to 0.6% of GDP taking only the ageing of the population into consideration, but to a level of 2.2% of GDP when also considering rendering the Estonian standard of living and the coverage rate of longterm care services more similar to the levels of the other member states by 2050. Similarly, the World Bank recommended increasing the financing of long-term care in Estonia in 2017 in order to adjust to an increase in the need for care. At the time of completion of the study, the public sector contributed nearly 100 million euros per year to long-term care, but additional financing would require the addition of a further 150 million euros every year.

The expenses on long-term care in society above all depend on the need for care. This means that society incurs expenses both when they are paid for jointly from public funds, and when people pay for care from their own funds. The increased contribution of the public sector to the financing of long-term care should not be avoided merely with the expectation of keeping the share of the public sector in the economy as well as the overall tax burden low. This is emphasised by the fact that the majority of long-term care is provided by close relatives whose absence from employment means that society and households still incurs expenses. In 2018, such expenses were estimated to amount 30 to at least 0.12% of GDP in Estonia (World Bank, 2017). (According to the estimate of the European Commission, such expenses as a whole in Europe may amount to 0.5% of GDP).

Like other countries, Estonia also combines different sources for financing long-term care. In Estonia, long-term care is mostly financed from the share of social tax in health insurance and from welfare financed from general budgetary income. However, due to the low level of public financing, the majority of the expenses on long-term care are borne by people and households from their own funds. Expenses incurred by people on account of their own funds are partially alleviated by saving up for old age via funded pension or buying a life insurance policy. However, the experience of other

countries should not encourage us to hope that the private insurance market will help save for and cover major expenses on long-term care.

The long-term care system in Estonia has been financed on a running basis. The burden of the decreasing population of working age for financing long-term care will increase in the future due to the ageing of the population. For the sustainable financing of major public expenses, possibilities for pre-financing should be considered, as this would save for a surplus of running costs on account of a diverse tax base rather than only labour taxes, which would help smooth out the tax burden and expenses on care over time. Pre-financing would increase the responsibility of the current generations to bear higher future expenses.

Financing long-term care in Estonia from both social security and general budgetary income helps prevent an excessive increase in the tax burden of the workforce. Compared to OECD member countries, we have comparable taxation of income and higher taxation of consumption while our taxation of entrepreneurship and ownership is lower. However, the financing of social security in Estonia is characterised by higher than average financing from social security contributions, i.e. labour taxes and contributions (approximately 75%, which is the highest indicator in the European Union). Additional financing of long-term care from labour taxes and contributions may increase the price of workforce and decrease the competitiveness of workforce. However, arising from the relatively small proportion of long-term care in public spending, the impact on labour taxes is not major – for example, if Estonia were to increase the spending on long-term care from the current level of 0.4% of GDP to 1.28% of GDP (the average level of EU member states) while also financing long-term care currently financed from general budgetary income from social security contributions, the social tax rate should be increased to 35.6%. It should be hereat considered that other social security expenses will also increase due to the ageing of the population, particularly in relation to healthcare, old-age pensions, and other social services that are related to age.

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