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Comments on the papers

1. The Income Concept in EU-SILC: Relevance, Feasibility, Challenges
   by Paul van der Laan, Statistics Netherlands

2. Comparability of income data across households/individuals and over time
   by Rolf Aarberge, Research Department, Statistics Norway

Paper prepared for the international conference on "Comparative EU Statistics on Income and Living Conditions: Issues and Challenges", Helsinki, Finland, 6-7 November 2006

The EU-SILC data are designed to study the distribution of income and well-being in each member state of the European Union, and to enable comparisons among countries. Paul van der Laan's paper deals with the income concept in EU-SILC, its relevance, its feasibility and the remaining challenges. This is a very fine paper that refers to all the EU recommendations and regulations that guide this EU-wide statistical exercise. The discussion of the income concept is mainly based on the recommendations of the so called Canberra group of which he himself was a member. I agree with his conclusion to focus the efforts on the quality dimensions of the surveys "accuracy, coherence and comparability". But I should like to add some points.

First let me note that the EU-SILC data are not representative of all the inhabitants of the member states. Although it is mentioned in the paper, which groups are missing, (the homeless, the population in institutions, and obviously the illegal inhabitants) I should like to emphasize that each country should at least produce estimates of the population shares of the resident population that are not covered by EU SILC, even if one does not know very much

about the living conditions and the well-being of these individuals. In addition to the total numbers at least the age and sex structure of this groups not covered by the surveys should be estimated, too. One could also expect that each country mentions in which institutions which shares of the population live. This information should accompany the EU-SILC data so that the users of these surveys can qualify their results. Remembering that the share of the elderly and of those in need of permanent care will continuously increase such information would become even more important in the future. One can even imagine an additional EU survey that describes the living conditions of the groups not covered by EU-SILC.

Second I should like to note that both papers do not consider the special problems of getting sufficient and reliable information about foreigners and about other persons with migration background that live in each country. Since the living conditions of this growing population group will become more and more important in politics it seems advisable to devote more resources per capita to the investigation of this group than to that for the indigenous population. Questionnaires in the most important foreign languages and bilingual interviewers might help. As is well known poverty rates can become very much biased downwards if the population group with migration background is not represented correctly.

I should like to stress a third point that is also made by Paul van der Laan. It is important to compare the grossed up sums of important variables, like market income, unemployment benefits, pensions, social assistance benefits and so on, with duly corrected aggregates of the National Accounts or of ESSPROSS, and to show which shares of these variables are covered in each country by the surveys. For some transfers this can and should also also be done with the number of recipients.

Paul van der Laan advises that special attention should be paid to the treatment of negative or strongly fluctuating income from self-employment. I should like to add that a retrospective question about the average incomes of this type (including the income of farmers) during the past three years might be helpful. It would be useful to introduce an additional variable with these averages.

I should like to emphasize another point that is made by Paul van der Laan only in passing. That is the use of only one equivalence scale, namely the modified OECD equivalence scale. At least for Germany it can be shown that this scale does not correspond to the scales that are implied in social benefits for households of different size, which are decided by Parliament.

Although the use of a single scale for all the member states may not make much difference for the results of the summary distribution measures, it has a great influence for the results concerning subgroups, and especially for their poverty rates. As a first step, I suggest, therefore, that all the indicators should be calculated alternatively with the modified OECD scale (1.0, 0.5, 0.3) and with the old OECD scale (1.0, 0.7, 0.5). These two scales seem to encompass the range in which the implied scales of the member states lie. This hypothesis can be checked by using the information given by the regular publication of all the social protection regulations of the member states in MISSOC.

Rolf Aaberge states at the beginning of his paper: "An underlying assumption for the meaningfulness of comparing and ranking a set of income distributions according to the degree of inequality is that the assessment carries over to the distributions of well-being. This requires that there must be insignificant interpersonal variations in the conversion of individual incomes into individual well-beings." This statement that refers to comparisons in general can be made more specific since there are seven different types of comparisons.

First, one can compare individuals in households of a specific country with respect to their relative position in the distribution of nominal incomes, and can calculate summary measures of income inequality and poverty. The individuals remain anonymous. For these calculations it can be assumed that errors in measurement compensate to a high degree. But these errors become the more important the smaller the subgroup for which these calculations are done.

Second, one can compare these summary measures of inequality and poverty for each country over time. In this case reliable statements about trends can be made even if there are errors in measurement provided one can assume that they remain approximately constant over time.

Third, one can aim at comparing the nominal income or nominal equivalent income of each member of a panel over time, which means that the comparison refers to identifiable individuals in a country that are only anonymous to the researcher for reasons of privacy. These analyses are most strongly influenced by errors in measurement at the individual level because one cannot distinguish them from real changes and because there will be no compensation of errors.

The fourth approach aims at a comparison of summary measures of inequality and poverty between countries. Obviously, such a comparison does not refer to the absolute levels of nominal or real income but only to the relative positions of anonymous individuals. But these comparisons at the level of disposable income in addition to the errors in measurement can be biased because of different systems of social protection. I come back to this point later on.

The fifth perspective aims at a comparison of the changes of relative positions of members of a panel in different countries, presumably condensed in some summary measures of income mobility, and measures of income mobility for certain groups, e. g. the initially poor population. Such a comparison shows the degree of stability of the various strata of society in the countries under review.

These five perspectives of comparison only refer to relative positions defined by one of the nominal income concepts in each country separately. They do not deal with absolute levels of nominal or real income.

As a sixth approach one can compare absolute levels of real incomes between countries by recalculating nominal incomes with purchasing power parities keeping in mind the limitations of such comparisons[1]. This approach shows differences in average and median real incomes between entire populations and – perhaps more interesting – between sub groups within each population.

The most ambiguous seventh approach consists of a ranking all individuals of all the member states by their real incomes within a single distribution and of calculating summary measures for the entire EU and, additionally, interpret the changes of these measures over time.

The comparison between countries of summary distribution measures based on real incomes, however, does not give new insights, if all the nominal incomes in each country are corrected by the same index of purchasing power. Only if group-specific indices of purchasing power are used, additional insight can be gained. This is one of the problems Rolf Aaberge deals with.

[1] Compare Appendix 3 of the study of the Canberra Group

The Canberra Group on whose recommendations Paul van der Laan mainly based his discussion of the income concept did not recognize clearly the differences in the social protection systems of the countries to be compared[2]. Since universal coverage of the entire population for the main social risks by mandatory systems does not exist in all the member states[3] the measurement of well-being by the proxy of equivalent disposable income is biased. This is especially important with respect to social risks that can hit everybody: Sickness, accident, old age and the need for care. This means that the well-being of the group of individuals who do not provide privately for these risks is overestimated by disposable income as defined by the Canberra group contributions. To improve comparability it is necessary to deduct from disposable income fictitious contributions for an adequate private insurance the benefits of which are comparable to the mandatory systems. This corrected income concept can be called "social risk corrected disposable income".

Rolf Aaberge's paper deals with a kind of metadiscussion referring only to Norway because

- he introduces an extended income concept in line with a Hicksian definition of income,
- he analyses the Norwegian income distribution comparing the results based on a standard income definition and his extended definition, and
- he introduces regional aspects into the measurement of poverty.

The results Aaberge derives are based on tax registers and additional registers that are available in Norway. They contain much more information than can be expected from the EU-SILC surveys. The Hicksian definition of income, for instance, includes imputed returns to assets the calculation of which needs information on the value of assets, and of the changes in their values. Since this information is not available with EU SILC, the Hicksian concept cannot be used for EU-wide comparisons. Therefore, I refrain from a discussion of the merits of this concept compared to the concept used in Paul van der Laan's contribution.

Rolf Aaberge also opens up a new line of criticism when he addresses the problem of regional differences within a country with respect to the price level and even to the prices of specific goods, and to average incomes of regions from which regional poverty lines can be derived. Obviously, this criticism can be extended, on the one hand, by distinguishing smaller and

[2] The Canberra Group mentions social security contributions to private schemes but it includes only contributions actually paid (comp. the discussion on p. 138). Here we are recommending imputed contributions for those who did not make provisions.

smaller regions within a country, and on the other hand, by applying it to comparisons between countries. This would mean that purchasing power parities have to be differentiated by regions within countries. Additionally, one has to decide whether to use a single country-wide poverty line or even region-specific poverty lines within each country. From a puristic point of view this critique is valid.

It is well-known that price indices and purchasing power parities calculated country-wide can only be considered an approximation to determine the real incomes of individuals. This problem also extends to the use of equivalent disposable *real* income as a proxy for the well-being of individuals. But given the fact that regional price indices and other regional information are not available one has to live with this critique keeping in mind a possible bias.

There is one way to partly take account of this critique that is feasible with the data of EU SILC. One could introduce an additional refinement of the income concept by subtracting housing costs from disposable income, and call this new income concept "free disposable income" (in addition to the correction for the non-universal coverage of important social risks.). Obviously, the poverty line would also have to be corrected by deducting average housing costs from the original poverty line to get a refined poverty line. Moreover, the equivalence scale has also to be adjusted. The calculation of summary distribution measures and poverty measures for each country and comparisons of countries could then be based on this refined income concept.

If one also wants to compare absolute levels of real income purchasing power parities excluding housing costs have to be used. Since housing costs are presumably the most important cause for within-country and between-country differences in purchasing power of nominal income such a procedure can weaken the critique mentioned by Rolf Aaberge.

[3] Compare MISSOC 2004

References:

Europäische Kommission (2004), MISSOC –Soziale Sicherheit in den Mitgliedsstaaten der Europäischen Union, im Europäischen Wirtschaftsraum und in der Schweiz, Luxemburg (Stand 1. Mai 2004)

Expert Group on Household Income Statistics – The Canberra Group (2001), Final Report and Recommendations, Ottawa