

The mandatory evaluation of adequacy of basic social security in Finland and how to improve it

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Introduction

An exceptional piece of legislation entered into force in Finland in 2010. The Ministry of Social Affairs and Health was to commission an independent evaluation of the development of the adequacy of basic social security every fourth year. The initiative arose from research-based knowledge on how the level of benefits may, in the long term, decrease significantly compared with the average income development, even if the benefits' purchasing power is guaranteed with index protection. A regular and periodic evaluation of basic social security was introduced as a way to obtain tested knowledge to support decision-making on the adequacy of basic social protection. Other important objectives of the evaluation were to provide support for budgetary processes and to follow up on the implementation of the government programme.

Two evaluation reports have been published since 2010 (Perusturvan riittävyden II arviointiryhmä, 2015; THL, 2011). In the first report, the key definitions were agreed, the guidelines were drawn up, and the development of a standard family's disposable income was studied over a twenty-year period. In the second report, the time series of disposable income development was shorter, but several new approaches to the question of adequacy were introduced. A long time series of the development of the benefit level and statistics for the benefit recipients were presented in both reports. The second evaluation report was also translated into English for the benefit of international audiences (SEGEABSS, 2015). In this paper, we shall first clarify the background of the mandatory evaluation. We then describe the analysis and present the main results of the two published reports and, finally, we introduce some of the planned improvements to be included in the third evaluation report.

The background and assignment

In 2007 the Ministry of Social Affairs and Health appointed the Committee for Reforming Social Protection (SATA Committee) to prepare a comprehensive reform of the social security system, which was seen as too complex and inefficient (SATA Committee, 2009). The candid aims of the committee were to simplify the system, enhance work incentives, and simultaneously alleviate poverty in an efficient way and nevertheless guarantee a decent degree of living. One of the conclusions of the committee was, however, that the income level guaranteeing a decent standard of living cannot be defined solely scientifically, rather being a matter of political perceptions.

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To ensure that the political decisions to be made are based on reliable statistical and scientific information, the committee proposed a periodical comprehensive evaluation of basic social security. The Ministry of Social Affairs and Health was to appoint an independent research group every four years so that the evaluation report would be available before the parliamentary election. The evaluation was to include 1) the development of a benefit level that related to consumer prices, to a 'decent' consumption level, and to wage levels, 2) an opinion poll of the adequate level of basic benefits, and 3) the development of work incentives. However, several issues were left to the consideration of the evaluation group.

The definition of basic social security is not clear-cut in Finnish discourse. Typically, it is seen to include all flat-rate benefits: the national pension as well as the flat rate unemployment and parental benefits, i.e. basic unemployment and parental allowances. Sometimes the list of basic social security benefits is supplemented with the minimum sickness allowance, student financial aid, child home care allowance, and survivor benefits. Since the assignment was to examine not just individual benefits but the sum of all factors contributing to basic means of support, the comprehensive set of benefits that is basic social security is complemented with housing benefits and last-resort social assistance.

The analysis

In the first evaluation report (THL, 2011) a working definition for basic social security was introduced. Basic social security was defined as the primary income security for non-active (those outside the workforce) persons not covered by earnings-related benefits. This primary income security is complemented by housing benefits and social assistance for people with the lowest income. A household's income formation was examined in four standard family types. The examinations were conducted in terms of disposable income both before and after housing expenses. Following the assignment, the adequacy of household income was evaluated in relation to the development of prices and wages, in relation to the reference budgets describing minimum consumption, and in relation to popular opinion. The income distribution status of those living on basic social security was examined and the level of Finnish social assistance was compared internationally.

In the second evaluation (SEGEABSS, 2015) both the model-family and the data-based analyses were deepened in many respects, nevertheless keeping the basic structure similar to that of the first evaluation. The model-family analyses were broadened by analysing the effects of housing costs at four different levels, rather than just one. Popular opinion on the adequacy of basic social services was now surveyed according to each benefit separately. Furthermore, the income distribution effects of the legislative reforms of benefits and taxation was evaluated using the new SISU microsimulation model maintained by Statistics Finland and the Research Department of the Finnish Social Insurance Institution (Kela).

The relative level of benefits

Table 1 presents the calculated level of disposable income for different family types after housing costs in comparison to the average-earning household's disposable income ('average-paid worker' in the table) in the period 1990–2015. Housing costs are assumed to be at the level of a rental flat in a medium-sized city. Detailed information on the assumptions behind the model family calculations can be found in the original evaluation reports (SEGEABSS, 2015; THL, 2011).

The calculated disposable income levels after housing costs of the basic social security recipients has decreased in relation to similar average-paid workers' households for almost all household types and all life situations since 1995. The decrease varies between 3 and 27 percentage points, being most considerable for a pensioner couple with two children. However, it has to be noticed that the assumptions of the two evaluation reports differ slightly, so the shares are not directly comparable, although the direction seems to be clear.

Table 1. Example households' disposable income after housing costs compared to similar, average-earning households' income ('average-paid worker') in 1990–2015 (%).

Family type	Life situation	1990	1995	2000	2005	2010	2015 ¹
Single-dweller	Unemployed, basic security	35	39	30	25	24	27
	Pensioner, basic security	37	41	34	29	27	34
	Minimum sickness allowance recipient	35	39	30	25	24	27
	Student in higher education	35	42	31	25	24	27
	Unemployed, earnings-related security	42	39	36	31	28	31
	Low-paid worker	55	46	49	47	47	53
	Average-paid worker	100	100	100	100	100	100
Single parent, one child	Unemployed, basic security	50	56	44	40	36	43
	Pensioner, basic security	46	62	50	44	41	43
	Minimum sickness allowance recipient	48	56	44	38	36	43
	Single-parent survivor	48	57	48	43	40	43
	Student in higher education	50	59	50	42	39	43
	Child home care allowance recipient	50	60	44	38	36	43
	Unemployed, earnings-related security	61	66	56	50	45	50
	Low-paid worker	70	72	66	62	59	68
Average-paid worker	100	100	100	100	100	100	
Couple	Unemployed, basic security	29	30	24	20	19	20
	Pensioner, basic security	28	34	28	24	23	29
	Minimum sickness allowance recipient	28	30	24	20	19	20
	Student in higher education	38	45	36	30	27	28
	Unemployed, earnings-related security	39	34	31	27	26	28
	Low-paid worker	52	50	51	51	51	52
	Average-paid worker	100	100	100	100	100	100
Couple, two children	Unemployed, basic security	46	51	40	35	32	36
	Pensioner, basic security	65	65	47	38	32	38
	Minimum sickness allowance recipient	47	51	40	35	32	35
	Student in higher education	52	52	43	36	33	36
	Child home care allowance recipient	47	51	40	35	32	35
	Unemployed, earnings-related security	53	55	46	41	36	41
	Low-paid worker	55	58	52	53	52	57
	Average-paid worker	100	100	100	100	100	100

Notes: The assumed type of housing is a rental dwelling in a medium-sized city. Source: SEGEABSS, 2015, p., 95; THL, 2011, p., 80.

¹The assumptions of the second evaluation report's example calculations may differ slightly from previous ones.

Table 2. Reference budgets of the model families in 2011 and 2014 (in EUR) and the disposable income after housing as a % of reference budgets.

Family type	Life situation	Reference budget, EUR/month		Disposable income / ref. budget, %	
		2011	2014	2011	2014
Single-dweller	Unemployed, basic security	660	675	63	71
	Pensioner, basic security	575	605	101	102
	Minimum sickness allowance	660	675	63	71
	Student in higher education	660	675	63	71
	Unemployed, earnings-related security	660	675	78	86
	Low-paid worker	660	675	129	132
	Average-paid worker	660	675	274	271
Single parent, one child ¹	Unemployed, basic security		920		90
	Pensioner, basic pension		920		100
	Minimum sickness allowance		920		90
	Single parent surviving spouse		920		90
	Student in higher education		920		90
	Child home care allowance recipient		920		90
	Unemployed on earnings-related security		920		105
	Low-paid worker		920		134
	Average-paid worker		920		214
Couple	Unemployed, basic security	1113	1143	64	73
	Pensioner, basic pension	1113	1143	99	104
	Minimum sickness allowance	1113	1143	64	71
	Student in higher education	1113	1143	92	102
	Unemployed on earnings-related security	1113	1143	89	99
	Low-paid worker	1113	1143	179	182
	Average-paid worker	1113	1143	350	351
Couple, two children	Unemployed on basic security	1698	1874	74	76
	Pensioner on basic pension	1698	1874	89	80
	Minimum sickness allowance	1698	1874	74	75
	Student in higher education	1698	1874	74	78
	Child home care allowance recipient	1698	1874	74	75
	Unemployed on earnings-related security	1698	1874	83	83
	Low-paid worker	1698	1874	120	113
Average-paid worker	1698	1874	233	216	

Notes: The assumed type of housing is rental dwelling in a medium-sized city. Source: SEGEABSS, 2015, p., 103; THL, 2011, p., 89.

¹ The family type 'single parent with one child' was not included in the reference budget scrutiny of the first evaluation report.

Among different household types, the relative level of disposable income was typically lowest for single-dwellers. The income of single-dwellers receiving basic unemployment allowance, minimum sickness allowance or student financial aid constituted 27 per cent of the corresponding average-earning single-dweller in 2015. The share had decreased considerably since 1995, by 12 percentage points. During

the last five-year period (2011–2015) the relative position of households receiving basic social security has improved. This is mainly due to the guaranteed pension reform in 2011 and the increases in the levels of social assistance and basic unemployment allowance in 2012. In addition, the development of earnings has been very weak since 2008.

The minimum reference budgets cover the basic needs of living and the goods required for the activities to satisfy the needs of a 'decent' level of consumption. In both evaluation reports the levels of disposable income of the different households were compared with minimum reference budgets defined by the Consumer Society Research Centre (Lehtinen & Aalto, 2014; Lehtinen et al., 2010). The housing costs were assumed to be at the same level as in rental housing in a medium-sized city.

Table 2 shows the share of expenses of the reference budget the model families are able to cover with their disposable income in 2011 and 2014 (SEGEABSS, 2015; THL, 2011). As with the wage level, the level of basic social security relative to reference budgets has increased from 2011 to 2014. For instance, the level of basic social security of a single-dwelling recipient of unemployment benefits, student financial aid or sickness allowance was enough to cover 63 per cent of reasonable minimum consumption in 2011, when in 2014 it accounted for 71 per cent. Respectively, the income of a single-dwelling guarantee pensioner covered 101 per cent of reasonable minimum consumption in 2011, and 102 per cent in 2014. The level of the single-dwellers' disposable income seems to be most insufficient of all households as obtained with this method.

The adequacy according to popular perception

Finns are particularly critical towards the levels of national pension, child home care allowance, and student financial aid, regardless of the year of inquiry according to the survey results presented in Table 3. However, other benefits of basic social security were also regarded as inadequate by the majority of the respondents.

Table 3. Popular perceptions on the adequacy of different benefits and reimbursements in the period 2000–2014. Share of those who consider the level fully or somewhat adequate (%).

Benefit	2000	2002	2003	2008	2011	2014
Health care reimbursements			48	42	49	60
Sickness allowance			49	46	43	57
Child benefit			42	37	40	57
Housing allowances	55	54	45	38	39	54
Labour market subsidy and basic unemployment allowance			35	33	30	46
Maternity or parental allowance			35	30	32	45
Social assistance					23	44
Student financial aid	37	31	30	24	23	38
Child home care allowance			27	22	21	36
National pension	35	36	33	20	20	34

Source: Kela and TNS Gallup, 2014; SEGEABSS, 2015, p., 105.

The benefits considered to be at the most adequate level have mostly remained the same during the studied period. These benefits are reimbursements for medical care, sickness allowance, child benefit and housing allowances. The top three benefits considered adequate in 2011 and 2014 are the so-called population-wide benefits, that is, income security regarding health care and child benefit.

There has been some change in opinions on the adequacy of benefits over time. When looking at the

changes between 2003 and 2011, it is evident that critical attitudes towards the adequacy of benefits have increased. The change has been moderate, but the trend is nevertheless clear. In contrast, between 2011 and 2014 the share of those who consider the level of benefits to be adequate has increased.

Work incentives

The inspection of work incentives was expanded and deepened considerably in the second evaluation report. Between 2011 and 2015, the work incentives for becoming employed full-time have become weaker. Table 4 shows that the average participation tax rate of becoming employed full-time has gone up by 3.5 percentage points between 2011 and 2015. The participation tax rate rises when the disposable incomes of unemployed persons grow faster than the disposable incomes of employed persons. There have been many reforms between 2011 and 2015 that have improved the financial situation of the unemployed, but also weakened the incentives of becoming employed. For example, the basic share of unemployment security was increased by EUR 5.62 per day in 2012.

Table 4. Average participation tax rates according to legislation in 2011 and 2014.

	2011	2015	Change (percentage points)
Unemployment → Full-time employment	59.4	62.4	+3.5
Unemployment → Part-time employment	64.2	59.7	-4.5
Part-time employment → Full-time employment	54.6	66.2	+11.6

Source: SEGEABSS, 2015.

Tax reliefs improve the incentives of becoming employed when they are targeted at income from employment. For instance, increasing the standard tax credit for work income in state taxes has improved the incentives of a person with low income to accept employment. The basic deduction in municipal taxes is directed at both income generated from employment and from allowances, which makes it neutral in terms of incentives for becoming employed at very low levels of income. Participation tax rates at higher levels of income, where the basic deduction is no longer applicable, rise along with increases in the basic deduction (SEGEABSS, 2015).

The exempt amount of EUR 300 per month for earnings in unemployment benefits, introduced in 2014, improved the profitability of part-time employment for low income wage earners. It did, however, also weaken the incentives for transitioning from adjusted unemployment benefits and part-time employment to full-time employment. The exempt amount to be introduced into general housing allowance will have similar effects on the incentives of employment (SEGEABSS, 2015). Between 2011 and 2015, the average participation tax rate has gone down by 4.5 percentage points when transitioning to part-time employment. On the other hand, the incentives of transitioning from part-time employment to full-time employment have become weaker and the average participation tax rate of transitioning from part-time to full-time employment has risen by 11.6 percentage points.

Improving the evaluation: the now-casting of the inequality indicators

The third evaluation has to be completed by March 2019. In the next round, our effort will be focused on improving the use of poverty and income distribution indicators. The micro-simulated decision-based income distribution effects were introduced for the first time in the second evaluation. For the third evaluation (2019), we propose that the scrutiny be expanded to the now-casting of the data to obtain the total impact of legislative reforms of taxation and benefits combined with the structural changes in the popula-

tion and the economic situation. The statistics on income distribution and poverty are always at least a year or two old due to data collecting procedures, thus a reliable method for estimating the current situation is required.

The indicators to be studied will be the at-risk-of-poverty rate and the Gini coefficient. The at-risk-of-poverty rate is defined as a percentage of the population living in households with equivalised income less than 60 per cent of equivalised median income, following the definition of EUROSTAT. It should be noted that Statistics Finland uses the expression ‘low-income rate’ instead of at-risk-of-poverty rate. The Gini coefficient measures the differences in the income distribution, usually scaled from 0 to 100. The higher the value of the Gini coefficient, the larger are the income differences (OECD, 2008).

The data used in the following calculations is a representative register sample of the total income distribution data of Statistics Finland. The data has been modified for the requirement of the SISU microsimulation model (SISU microsimulation model, 2013). It consists of the extensive socio-economic details of 800 000 persons.

We first estimated the decision-based income distribution effects. The disposable income of households in the 2012 population data were simulated with the SISU microsimulation model according to the tax and benefit legislation in 2011–2015. In this way we were able to isolate the direct income distribution effects of policy changes from other changes affecting income differences, such as those in the population structure. The monetary parameters of legislation have been adjusted to the level of the data year with the earnings-level index, which means that the slower growth rates of social benefits in comparison to earnings are interpreted as decision-based changes. A similar method has been used in earlier studies evaluating the income distribution effects of policy reforms (e.g., Bargain & Callan, 2010; Honkanen & Tervola, 2014).

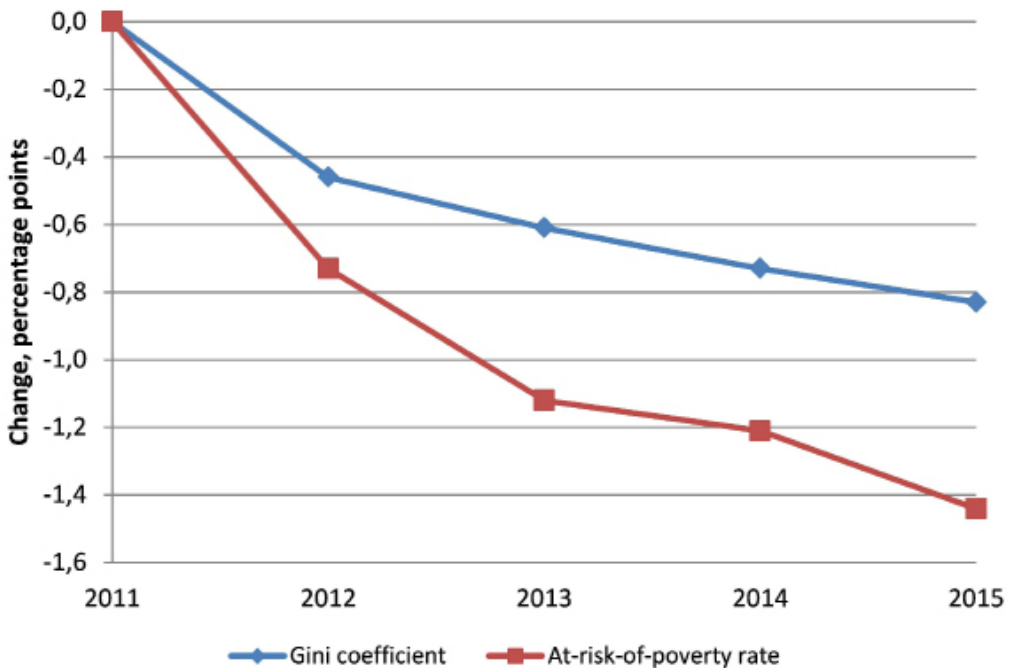


Figure 1. Effect of legislative reforms on the Gini coefficient and at-risk-of-poverty rate in 2011–2015. (Source: SEGEABSS, 2015).

Figure 1 presents the estimated effects of reforms in benefit and tax legislation in the period 2011–2015 on the Gini coefficient and the at-risk-of-poverty rate. Overall, the changes made in benefits and taxation in 2011–2015 have reduced the income differences and the at-risk-of-poverty rate. The reforms in benefit and tax legislation have reduced the Gini coefficient altogether by approximately 0.8 percentage points and the relative at-risk-of-poverty rate by approximately 1.4 percentage points.

The tax-benefit microsimulation model is a detailed and substantial instrument for the model family calculations, the decomposition method, and for evaluating the impact of policy reforms (De Agostini et al., 2014; Callan et al., 2011; Cantillon et al., 2014; Honkanen & Tervola, 2014; Matsaganis et al., 2007; Moisiu et al., 2016). However, simply applying the calculation rules corresponding to the legislation on the aged data does not take into account changes in the population structure or in the economic situation, even if the changes were substantial. One solution to access more accurate estimates for the current situation is using the so-called ‘now-casting’ method to bridge the time gap between the current year and the year the data represents (Bourguignon & Spadaro, 2006; Immervoll et al., 2005; Leventi et al., 2013; Navicke et al., 2013).

In the now-casting process the base data was modified to represent the situation in the year of interest by means of a complicated weighting process. The components of the population structure taken into account are population size, distribution of gender and age, number and structure of households, number of wage earners, earnings-related pension receivers and unemployed people, number of days receiving earnings-related unemployment allowance, number of days receiving basic unemployment allowance, and days receiving labour market subsidy. This procedure is called re-calibrating the data. The re-calibration as well as the monetary increases are performed with the Swedish now-casting program CLAN97 (Andersson & Nordberg, 1998).

Table 5 presents the development of the at-risk-of-poverty rate in the period 1995–2014 and the now-casted estimate for 2015. The at-risk-of-poverty rate was 12.5 per cent in 2014 according to official statistics. Simulation with the now-casted data estimates that the poverty risk rate will decrease circa 0.2 percentage point from 2014 to 2015, leaving the at-risk-of-poverty rate at 12.3 per cent.

In 2014, the Gini coefficient was 25.2 in Finland according to official statistics. In Table 5, it can be seen that the Gini coefficient estimates obtained by the simulations with now-casted data indicate an increase of 0.5 percentage point between 2014 and 2015, the estimated Gini coefficient being 25.7 per cent in 2015.

Table 5. At-risk-of-poverty rate and the Gini-coefficient according to statistics (years 1990–2014) and now-casted estimates for 2015.

	1990	1995	2000	2005	2010	2011	2012	2013	2014	2015
At-risk-of-poverty rate	10.5	7.6	10.5	12.7	13.7	13.2	11.9	12.8	12.5	12.3
Gini coefficient	20.8	21.4	24.9	25.9	25.9	25.9	25.5	25.6	25.2	25.7

Source: Statistics Finland (2016) and own calculations with the SISU microsimulation model.

Summary and discussion

The mandatory evaluation aims to provide a research-based perspective on the development of the adequacy of basic social security. A regularly performed evaluation estimates the effects of the reforms and the level adjustments made during the past parliamentary term. Even the benefits linked to the National Pensions Index, thus being protected from inflation, have a tendency to decrease over time in relation to wages. The value of a regular evaluation is even more relevant now that the the governmental programme

has frozen index increases for the period 2016–2019 (Prime Minister's Office, 2015, Annex 6, p. 36). The question of the adequacy of basic social security and its acceptable relation to the average standard of living in the population is value-based, but to be able to understand the effects of reforms, decision makers need objective information. The objective of the mandatory evaluation is to provide material to support political decision-making relating to these core questions of social policy.

In summary, the main results of the two evaluation reports suggest that the level of basic social security has improved both in real terms and relatively compared to average wages in 2011–2015, but the level is still not adequate to cover reasonable minimum costs as determined in reference budgets. Work incentives have weakened over the period 2011–2015. In the longer 25-year perspective, the relative level of basic social security compared to average wages has declined substantially. Popular perceptions on the adequacy seem to be in line with these results; roughly half of the population sees the level of basic benefits as inadequate.

In the second evaluation report, the impact of tax-benefit reforms was estimated for the first time. Policy reforms in the period 2011–2015 narrowed income inequality and lowered the at-the-risk-of-poverty rate according to the results obtained with microsimulation modelling. However, as we have seen earlier in the paper, the impacts of decision making should be scrutinized more closely by also taking into account the changes in the economic situation and the structural changes in the population, not just concentrating on the legislative reforms. We have introduced now-casting as a candidate for this task in the third evaluation in 2019. Our analysis indicates that it is necessary to make the adjustments on the data to be able to consider the total impact on poverty and inequality, rather than simply applying the current legislation on data that is several years old.

There is strong demand for a regular evaluation of the adequacy of social security. Both the evaluations in 2011 and 2015 sparked vivid public debate, where the results were discussed in newspaper editorials inter alia. Especially the 2011 report turned the public and political spotlight on the long relative decline of the level of basic social security in Finland between 1990 and 2010. The results of the report were used to justify the basic security increases in parliamentary debates in 2012. Nevertheless, Prime Minister Sipilä's government, which began its term in office in 2015, has introduced several retrenchments in social policy on a scale not seen since the early 1990s (Prime Minister's Office, 2015). The impact of these alignments and reforms will be evaluated in the third evaluation in 2019.

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