Household production and Social Security: the case for a Social Divorce Insurance

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1. Motivation

- Following divorce or a separation, many parents and children face poverty
  - 36% of lone parents live ‘at risk of poverty’, while
  - 10 to 20% of couples with children do (BE,2014)
  - Child poverty may have long-lasting consequences
- Two main causes of poverty:
  - Maintaining two households is more expensive than one
  - Alimony default is widespread

Maintaining two households: disadvantages of scale

- Though living standards differ strongly between households, larger households are enjoying advantages of scale over smaller households
- It is commonplace (e.g. Eurostat) to use ‘equivalence scales’ to compare households of different composition. An example (2+2)
  - Before: household of four 2,1 = 1x1 + 1x0,5 + 2x0,3
  - After: household of one 1,0 = 1x1
  - After: household of three 1,6 = 1x1 + 2x0,3

Alimony default: failing private solidarity

- Alimony is private solidarity
- Partners are forced to take care of each other's well-being, even when deciding to separate
- The economically stronger party (often man) is expected to transfer income to the economically weaker party (often woman)
- In reality, payments are often not made or are delayed
- Moreover, not all 'stronger' parties earn enough to transfer a significant amount

Prospect

- Luckily, poverty among lone parents is most often not persistent:
  - Lone parents re-partner
  - Lone parents become economically stronger (mostly: work more intensely)
- A temporary income transfer may avoid many problems

Why not anticipated? A social risk

- Poverty rates show that income loss is unexpected and/or badly anticipated
- Economically rational individuals, would – when engaging - take a private insurance to cover them for the likelihood of an additional income need when/if hit by a separation
- Reality shows a typical example of the common human tendency to underestimate the probability of relatively likely life events
- The involvement of children makes it transcend the purely individual decision arena.

Social insurance: forcing all citizens to contribute

- Avoids ‘free riding’
- Avoids lack of coverage
- Distributes risk at the maximum, obtaining the lowest possible contribution fee

- Social separation insurance covers a new social risk, based on principles similar to health, old age and unemployment insurance (the ‘old’ social risks)

The benefit of the social separation insurance

- A temporary benefit
- ‘Gives people a break’ in emotionally turbulent times
- Avoids most pressing income consequences after a separation or divorce

Design issues

- Being a social, obligatory insurance, the separation insurance avoids *“adverse selection”,* a problem of private insurance systems which tend to attract persons with “bad risks”.
- In common with other (private and social) insurance systems, the separation insurance will have to confront *“moral hazard”,* the tendency of (some) insured people to become less cautious towards the risk.

Types of moral hazard

- Some partners may seek separation, because they like the prospect of an insurance benefit. Consequently, the insurance may raise the separation rate (‘risk seeking’)
- Separated individuals may not be motivated to take action, to confront the problems caused by their separation (‘complacency’)

Regarding risk seeking

- Safeguard 1: one may hope that money does not trump emotional well-being (a separation is not just an economic event)
- Safeguard 2: checks regarding the true living situation are required to avoid “fake separations”, in common with all other benefits that depend on the household structure
- Safeguard 3: the benefit should be temporary to contain the “attractiveness” of the benefit (maximum accumulated benefit over full period)

Regarding complacency

- Safeguard 1: the benefit is temporary
  - like unemployment benefits
  - motivating people to get organised
- The duration may be ‘socialized’, i.e. depend on the employment rate of similar individuals (e.g. number and age of children). Thus it reflects
  - social reality & expectations
- Safeguard 2: the amount is decreasing over time
  - again like unemployment benefits
  - yet, the incentivizing effect of this decrease is debated

Basic trait: Income insurance

- Covers income lost, i.e. the loss of ‘equivalent income’ because of the formation of two households rather than one.
- Has socially acceptable minima and maxima (cfr. limits of old age pension benefits)
- Is not conditional on income: it avoids the use of social welfare for the duration of the benefit.
- Postpones alimony regulations: during the benefit period, alimony is “socialized”, paid for by the solidarity mechanism of the social insurance, rather than private solidarity.

Conclusion and discussion

- Separation is a new social risk
- It is badly anticipated by many citizens
- It is poorly responded to by the welfare state. Measures covering alimony default and residual welfare systems do not avoid high rates of (child) poverty among lone parent households
- A new social insurance may be called for
- *Remaining question*: is the climate ripe for this new social contract?