

The Economic Psychology of the Welfare State

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EFI THE ECONOMIC RESEARCH INSTITUTE



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PREFACE

This report is a result of a research project carried out at the Institute for Economic and Business History Research and the Center for Media and Economic Psychology at the Economic Research Institute at the Stockholm School of Economics.

This volume is submitted as a doctor's thesis at the Stockholm School of Economics. As usual at the Economic Research Institute, the author has been entirely free to conduct and present his research in his own ways as an expression of his own ideas.

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Stockholm January 26, 2009

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Without a deep understanding of the Swedish political history this thesis would not have been possible, I must therefore thank all those that have helped me improve my understanding of this field. As much of what occurred in this field was never put on paper – especially regarding the early phases of the political processes covered in articles 3 and 4 – I am most grateful to all the former politicians, officials and civil servants – mentioned in the bibliography– that have shared insights with me during interviews and conversations.

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Stockholm, January 2009

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Introduction

If the period ending in 1950 can be said to have been the *formative phase* of the Swedish welfare state, the period between 1950 and 1975 constituted its *expansion phase*. During the formative phase it was often the local community – the parish or the municipality – that produced services, such as schools, care for the sick and for the old. The municipalities were also responsible for the police force and the enforcement officers. The expansion phase that followed meant sharply increased public commitments, and increased centralization. During this period, the national government took over responsibility for many activities which had previously been handled locally or regionally, e.g. the police force, the courts and the schools. The reform of the municipal system that took place during this period also had as a consequence that the number of municipalities was significantly reduced. At the same time their size increased; thus there was centralization even at the municipal level. After 1975, the expansion of the public sector slowed down or ceased and the changes made concerned primarily responsibility and efficiency. It is this latter period – the *consolidation phase* of the welfare state – which is addressed in this dissertation. Even if the expansion of the public sector ceased at the national level, it continued in the municipalities. The rapid expansion of child care was the clearest example, but other municipal activities also expanded in scope.

At the end of the 1980s, a big wave of changes was initiated in the public sector. Several important activities were transferred from the central government and the counties¹ to the municipalities. The most comprehensive changes concerned the schools and Elder Care, the responsibilities for which were transferred to the municipalities in the early 1990s. Other activities, such as care of the disabled, were also transferred to the municipalities during this period. Somewhat surprisingly, none of these changes were of an ideological nature. On the contrary there was a consensus across party lines about the general direction of these decisions, even if the details were debated.

On the taxation side, there were also large changes. At the end of the 1980s, public expenditure increased markedly and this was followed by corresponding increases in the tax rates. In article two, a specific effect of these tax increases will be examined, i.e. those cases where municipal politicians increased taxes more rapidly than the economy was growing. The hypothesis is that such tax increases had a disproportionately large negative impact on the election results for the ruling party or coalition. This assumption implies that such tax increases should be rare. Indeed they were. However, they did occur, most of them 1988-1994. A likely explanation is the rapid rate of increase in the expenses during this period (both at the end of the 1980s and the increase caused by the economic crisis in the early 1990s). This period was also influenced by the restructuring of the tax system. The tax reform of 1990 brought a serious reduction in the marginal income taxes at the same time as the Value Added Tax ("VAT", a form of sales tax) was increased. An approach using economic-psychological theories could potentially explain the electorate's reaction to the changes, while an approach using a historic theory is required to explain why the politicians acted as they did.

1 Throughout this thesis "county" is used as translation for the Swedish "landsting".

Placing this dissertation into a specific category is not possible. Instead, the approach is to use theories and methods from different research traditions in concert. The dissertation has an overarching goal: to give examples of how it is possible to improve the understanding of historical events, by using economic-psychological theories as tools.²

This thesis is partly about institutional change. This, however, do not imply that institutional theory by necessity is the only tool that could be used to analyze these changes. Institutions can influence decision making in organizations. One could e.g. argue that it was necessary for the opposition qua opposition not to accept proposals from the Government. In this case, the institution “opposition” defined what could and could not be done. Organizational change can in turn drive institutional change.

There are a number of connections between institutional and psychological theories; the general one being that psychological effects can impact the shape of institutions and institutional change. There is however a basic difference between the two, even if there are variants of institutional theory that drops the assumption of perfect information and instrumental rationality (Ménard and Shirley, 2005). The regularities underlying economic psychology are assumed to be functions of what goes on in the heads of individuals (North 2005). They would therefore, in contrast to the contextual norms North includes in the definition of intuitions, be consistent over time and space.

Theory can be used in different ways. One way is to generate various hypotheses from the theory, and then test to what extent the theory fits the empirical data; another way is to assume that the theory is correct and use it to interpret empirical material. In this dissertation, theory is used mainly in the latter way. A multifaceted reality can support differing theoretical constructions. Therefore, this dissertation both gives a description of how the Swedish welfare state operates, as well as attempts to reach a better understanding of this mode of operation with the help of theories from economic-psychological research, by addressing some economic-historically interesting research questions.

Economic psychology is to a large extent based on formalized regularities that have been found in laboratory experiments. Therefore, it is often unclear whether the results thus obtained can be repeated in an uncontrolled environment. There is, however, strong support for the tenet that decision rules described by the theory can be observed even outside a laboratory setting. In research exploring how people act in the financial markets, economic-psychological theory is well established and the results that researchers have obtained by experiment have in many cases been verified with empirical, non-experimental data. It is likely that people will make decisions in a similar fashion regardless of whether the decisions are about how to invest their money, vote in an election, or how they regard income from a sale of stock or a cash grant from the government. Therefore, one could justifiably expect that the theory should be applicable even for political decision-making.

² In the field of economics, economic psychology is often called “behavioral economics” to distinguish it from classical – rational – economics. In this thesis economic psychology and behavioral economics are used interchangeably.

All studies of political decision-making also face the problem that it is not possible to see what goes on in the mind of the decision-maker and what constitutes their real motives. What a person says in an interview, writes in a bill in Parliament, or answers in an opinion poll is influenced – to varying degrees – by the norms of society, what is strategically or tactically useful to say at the time in question and so forth. Here, economic-psychological theory can function as a promising complement to traditional source criticism. When judging the value of a source, precision can be increased by looking at whether the data from the source corresponds to the predictions that are given by economic-psychological theory.

Research on political decision-making is often based on more traditional theories such as institutional theory (e.g. Coase 1960, North 1990, North 2005, Ménard & Shirley 2005), Public Choice and Rational Choice (e.g. Arrow 1968, Elster 1986, Buchanan 1959, Buchanan & Tullock 1962, Mueller 2003, Olson 1962) or on political science theories, for example Kingdon (1995) and Cohen, March & Olsen (1972). In the first two parts of this dissertation, the economic-psychological approach is contrasted against Public Choice. In articles 4 and 5, the economic-psychological approach is contrasted with, and complements, primarily institutional theory and theories from political science. There are certainly a number of other possible theories that can be formed and which could contribute to the understanding of the political sequences of events which are examined in this dissertation, but the primary objective is to try to improve the historical analysis with the help of economic psychology. The fact that other theories, that could give alternate explanations, are not studied here is not to be interpreted as they would lack explanatory power, but only that they are outside of the scope for this dissertation.

Delimitations and Sources

The source material for the two case studies is partly official printed sources, such as minutes from Parliament, bills introduced and government studies, and partly statements from the people that were participants in the decision making process. A number of people who were government ministers during the period in question have written memoirs, and all of those have been scrutinized during the preparation of this dissertation. A feature (or rather non-feature) those memoirs have in common that they either do not mention the reforms at all, or discuss them extremely briefly. One of those who do not mention the reforms in his memoirs is Ingvar Carlsson, the then Prime Minister (Carlsson 2003), and the then Minister of Education, Göran Persson (Persson 2007), discuss the transfer of schools to the municipalities using less than a page, while the transfer of Elder Care to the municipalities is not mentioned at all. This suggests that the decision makers who were involved in the process did not consider these reforms to be particularly important, despite the fact that together they constituted about a third of the obligations of the municipalities.

The written source material has been supplemented by personal interviews. The persons interviewed had central positions as decision makers when the deci-

sions about transfers of responsibility to municipalities were made, or else they had a good view into the specific decision process and/or knowledge about the overarching political process. The use of interviews is especially important as the rest of the source material largely concerns party politics of the immediate present at the time, and only to a lesser extent describes what went on outside of public view. It should be noted that the interviews give an image of a largely consensual process leading up to the two reform decisions. For the study of how changes in the levying of taxes influence the support of the electorate, the source material is a data base of tax and election results data, specifically developed for this purpose.

The processes of change that are described in the case studies have been selected by the following criteria: (i) they must have significant economic scope, (ii) they must be fairly non-ideological, and (iii) they must have taken place during a time recent enough that it was possible to interview some of the most important actors. The historical period in this dissertation is thus 1975-2002. The delimitation in time has as a result that all the political decisions that are studied were made after the municipal reforms were fully implemented and after the unicameral Parliament and the new constitution had been put into force. As a consequence, all the decisions were made within the same overarching institutional framework. It should also be noted that the two case studies concern decisions that were made before 1990. That means that the decisions in question are less coupled to current party-politically contentious questions.

One could justifiably raise the question why these particular cases were studied. There are many areas of interest to the researcher in economic history who wishes to study the processes of political change. The most far-reaching changes were most likely the municipal reforms during the 1950s and 1960s, which radically changed the conditions for public activities, and the ATP-system (government pension system funded by payroll taxes), introduced in 1960, which in one stroke increased the public commitments by a third.³ The municipal reforms at the time, like the later transfer to the municipalities of schools and Elder Care, were relatively non-ideological. The distance in time, however, makes it impossible to conduct interviews today. The ATP-issue is not suitable as a case study either, as there were hard-fought ideological battles between socialist and more market-oriented political forces over this issue. A further, but subordinate, criterion has been to study areas that can be said to be under-researched. The relative absence of previous research is most likely a consequence of the fact that these reforms were based on consensus about the goals, and therefore did not cause political strife.

The choice to write individual papers and create a larger study by collating them into a dissertation is motivated by the fact that it is then easier to focus on one specific issue at the time, and to use different research methods. The disadvantage of writing individual papers instead of a monographic dissertation is the need for repetition. In this dissertation this applies primarily to the two case studies, schools and Elder Care, which are based on the same theories and, in addition, have some source material in common.

³ Borg 2004, p 178f

Description of the Dissertation

This dissertation consists of four articles which in different ways use economic-psychological theories to explain and analyze historical sequences of events.

Article 1 – *Can Behavioral Economics Improve the Understanding of Politics?* – is an overview of current research and a description of how economic-psychological theories can be applied in economic history, and it also suggests areas where such an approach could be particularly promising. The article takes its starting point in commonly used theories of political conditions. It is argued that by adding insights from economic psychology a better analysis of historic processes is possible. Some connections are also made to sociobiology and to other areas of research within the natural sciences. The paper is primarily concerned with two issues; (i) why politicians sometimes push political policies which an overwhelming majority of the voters do not support, and (ii) whether there are psychological phenomena which make it easier to drive the political process in one direction than another. One explanation to the former phenomenon (which traditional theories often ignore) is that the politicians may believe that they have popular support for their policies. There are phenomena like *cascades* (Bykhchandani & al 1992, Kuran 1996, Kuran & Sunstein 1999), *encompassing sentiment coordination* (Klein 2005) and *self-serving biases* (Babcock & Lowenstein 1997) that can produce this result. It may either be the case that people closest to the politician support the policy, and that they simply do not encounter people with divergent opinions, or that the politicians simply believe that the voters have the same opinion as they themselves have because their position is the “correct” one.

The issue can also be approached with economic-psychological theories. If people act as predicted by *prospect theory* (Kahneman & Tversky 1979, Thaler 1980, 1985, Tversky 1981, Tversky 1992, Wakker & Tversky 1993, Rabin 2000, Rabin & Thaler 2001, Wahlund 1989, 1993) this will have an effect on how tax and welfare policies are shaped. For example, there will be inertia that makes it difficult to abolish social benefits once they are introduced. If the cost for these benefits increase (for example because the salaries in the public sector increase, or if the productivity decreases), this will lead to a growth of the public sector and a corresponding increased tax burden as it will be perceived to be more costly to decrease social benefits – a perceived loss – than to increase taxes – a perceived forgone gain. It can, however, be that if taxes are raised too much, this will be perceived by the electorate as a loss of income and thus cause resistance. (This specific hypothesis is formally tested in article 2.)

Proximity effects (Milgram 1963, 1965, Kilhan & Mann 1974, Latané 1981, Latané & Wolf 1981, Tanford & Penrod 1984, Trope & Liberman 2000) can also influence which policies are successful, but here restraining effects on the expansion of the public sector can be expected. A special category of psychological effects that can influence which policies are most easily accepted by the electorate are those that concern how the policies are formulated. This article discusses, among other things, the presence and the effects of “kin rhetoric” (Salmon 1998, Klein 2005). Studies show that political programs that are motivated in terms of

kinship get a more positive reception than those that are justified with by for example citizenship. According to socio-biological theories it is rational to help those to whom you are related because they share parts of your own set of genes. Policies that are dressed up in terms of that those who need “help” are related to us – but in fact are not – can therefore lead to exaggerated solidarity and to that certain policies become successful. In this case, it contributes to a bias to an expanding welfare state.

Article 2 – *Are you Better off now than you were Four Years Ago? Psychological Insights in Tax Policy and Voter Behavior* – is an econometric study of how the electorate in Swedish municipalities reacts to changes in fiscal policy. The starting point is the economic-psychological implication *loss aversion* and the hypothesis is that the electorate uses economic growth as a reference point when they evaluate municipal tax policy. Municipal politicians that increase taxes at a higher pace than the economic growth are thus assumed to lose electoral support to a much larger extent than those which have raised taxes at a slower pace. As a base for the study, new and extensive, data base containing municipal taxes and municipal election results has been created. The data base comprises all Swedish municipal elections from 1976 to 2002 in addition to the municipal tax rates for all municipalities during this period. In all, the data base contains 18 560 observations about election results and 5 510 observations about tax rates. For each municipality and election, the governing majority has been indicated. This differentiates this data base from earlier attempts to develop such data bases. In Petterson-Lidbom (2008) for example, the assumption has been that the coalitions – “blocks” – that compete for power always are comprised of the same parties. In reality, coalitions do not always look like that. Instead there are municipalities which are governed by coalitions reaching across block boundaries (i.e. containing parties from “both sides of the aisle”), or coalitions that contain parties that are not represented in the national Parliament, for example parties that are specific to a particular municipality or parties that have yet to achieve a breakthrough at the national level.

The size of the data base also enables us to do statistical tests of a different kind than what would have been the case with a smaller set of data. Additionally, it makes it possible to do more correct studies of electoral behavior because it covers a long period of time. Politics at the local level is likely influenced by economic and political macrotrends, and by studying a long period it is possible to allow for both the changes in the general economy – for example the oil crisis of 1979, the finance and real estate crisis 1990-1991 and the IT-crash 2000-2001 on one hand, and the political power shifts at the national level on the other. During the period studied, 1976-2002, Sweden was governed by a center-right coalition until 1982, and 1991-1994, and by the Social Democrat party during the other years, 1982-1991 and 1994-2002.

There is a large body of research concerning American elections where the connections between macro-economic variables, such as inflation and unemployment, and election outcomes have been studied. In this research, it has been possible to find a clear negative correlation during the period after WWII between these variables and the support of the electorate for the then-current president

(Barro 2004). These studies are, however, mostly of anecdotal interest since, as for one thing, there are relatively few data points (the US has had 16 presidential elections since 1945 and 11 different persons have been elected to the office) and for another thing, there are many variables that have not been controlled for.

When Ronald Reagan before the election 1980 asked the electorate if they were “*better off now than four years ago*” he captured a classical theme in politics. If the electorate is of the opinion that things are heading in the right direction (concretely: if they are better off) they are expected to support those that are in power at the time. If they believe that things are heading off in the wrong direction, they are expected to vote for change. Also the presence of loss aversion drives the electorate’s behavior in this direction. If the person casting a vote experiences that he or she is worse off, he or she will be more willing to take the risk of voting for a new alternative.

In a Swedish municipality there are much fewer variables that the local politicians can influence. The activities of the municipalities are largely governed by national legislation and the municipal politicians can only to a limited degree influence what kind of activities they will pursue. Additionally, municipalities are prohibited using methods of financing other than the proportional (“flat”) income tax, which is not deductible for the taxpayer for the purpose of calculating his tax liability at the national level. Furthermore, the number of municipalities is large and they all have the same electoral system. This makes Swedish municipalities almost ideal as objects of study for purposes such as these discussed above.

It would not have been possible to make the corresponding study at the national level: the number of elections is too small to get the necessary variation, and the issues that the national government can address are innumerable. For example, in contrast to the municipalities, the national government has a large number of sources of revenue, such as VAT, income taxes, “point” taxes on specific products (such as tobacco and alcoholic beverages), payroll taxes, “congestion taxes” (e.g. on cars entering inner cities), excise taxes etc., all of which can be levied and can be given certain exemptions. Parliament also has much larger latitude concerning decisions on how the tax money will be used.

The results of the investigation were clear. That governing coalition that raises taxes by more than the economic growth, i.e. such that the average voter can be assumed to have less money in his wallet, is punished by a drop of about 2.5 percentage points in the elections. On the other hand, it is not possible to find a significant effect on the support of the electorate from tax increases that are smaller than the economic growth or from the tax burden in general. The amount of variance thus explained is low, however, so even if the results are statistically significant, they are not necessarily practically significant. Even if caution is called for when trying to make prognostications, the result can be a partial explanation for why the Swedish welfare state has been able to grow to the extent that it has. One interpretation of the results is that small tax increases do not cost anything in terms of voter support at the same time that it is plausible to assume that the service that is financed by the taxes gives positive support. The study at the same time indicates that the electorate has a fairly short memory. Only tax increases that take place during the

year immediately preceding an election influences the support of the electorate, and then only tax increases that have been larger than the economic growth. Tax increases that, since the previous election, only cumulatively have exceeded the cumulative economic growth, on the other hand, have no significant influence on voter support.

A historian should be aware of how the observations made fit into the historical context. Even if the study gives a clear result, it should be noted that most tax increases that exceeded the economic growth took place during the period 1987-1994. This period is special from several points of view. During this period public expenditure increased massively, and it also coincided with the 1990s fiscal crises (where the government deficit reached 10 per cent of GNP). If the assumption is made that the politicians know that rapid tax increases would result in reduced support by the electorate, it should also be assumed that they would avoid them. The special conditions during the late 1980s and the early 1990s can serve as explanations of the fact that politicians, despite risking losing voter support, nevertheless implemented large tax increases. This does not make the results any less interesting, however.

In articles 3 *The Municipal Takeover of the School System* – and 4 – *The “Ädel” Reform: An Economic-psychological Analysis of the Transfer of Government Activities from Counties to Municipalities*, special cases of political decision-making are studied, i.e. the transfer of responsibility for public activities from one political level to another. Schools were transferred from the national government to the municipalities in connection with the 1991/1992 academic year, and Elder Care was transferred from the counties to the municipalities at the end of 1992. These reforms increased to a significant degree the areas of municipal responsibility. The distinguishing characteristic for these reforms was that they took a very long time to implement. The starting point for the transfer of the schools to the municipalities can be found around 1970 and the transfer of Elder Care has been discussed since at least the middle of the 1950s. Another distinguishing characteristic is also that there was wide-spread political consensus around both the definition of the problem and its solution. In spite of the fact that it likely was possible to assemble a Parliamentary majority for the transfers of both schools and Elder Care from the 1970s onwards, no such decision was made for a long time. When the issues were finally brought up in Parliament, there was however political dissent, but the disagreement was not primarily about the content, but about how the decision should be made, and when.

When the transfer of schools was imminent, there was a fairly large amount of debate in the media, where most especially the teachers' unions argued for the schools remaining as a continued national responsibility. A comparison between the image created by the media of the debate about transfer to municipalities with the image being created in the dissertation, the impression could be gathered that the two are not compatible. This is not the case. The article is concentrated on the political decision making process, whereas the media are an arena where different actors attempt to influence the decision makers in one direction or the other, and where the debate does not necessarily reflect the politicians' views. In spite of a

heated debate both in the media and in Parliament, the conclusion of the article is that there was a fundamental consensus about the underlying principles and that the debate there to a large extent was about procedural matters.

The two case studies also describe the economic results of the reforms. The economic results of the transfer of schools to the municipalities are, however, relatively difficult to isolate. From the late 1980s and onwards, a number of changes were made concerning schools: the teachers education was changed, the municipalities took over the responsibilities from the national government, the National Swedish Board of Education (*“Skolöverstyrelsen”*) was disbanded and replaced by the National Agency for Education (*“Skolverket”*), which also was given some additional tasks, the curriculum was revised, the system with school vouchers and independent schools was introduced, in the high-school system (*“Gymnasieskolan”*) the “line system” (science, humanities etc) was replaced by “programs”, and those “lines” that had previously been two-year lines were extended to three years. Additionally, a new grade system with goal-related grades was introduced. All these changes make it difficult to isolate the effects of transfer to the municipalities.

Without speculating too much, it should be possible to classify some results as due to the transfer of responsibility to the municipalities. The obvious effects are those that coincide with the transfer in terms of time, where the clearest effect is the break in the cost trend curve that followed the reform decision. Even those changes that were a direct result of the increase in the number of responsible parties should be classified as being caused by the transfer to municipalities. Among the changes that were a consequence of the transfer of the responsibility were those that are the result of the fact that it suddenly became possible to compare different municipalities. It is therefore likely that the large cost reductions in the handful of municipalities which had a cost level significantly exceeding that which was the case in the rest of the municipalities can be included in this explanation. When the municipalities themselves had to pay and at the same time could see that other municipalities with similar preconditions could achieve the goals at half the cost, it would likely have produced clear downward pressure on costs.

It is somewhat easier to isolate the effects of the “Ädelreform”, the transfer of Elder Care. During the period in question there were no other large changes concerning Elder Care. The Elder Care reform was also followed by clear break in the cost trend curve. It is also clear that the decrease in the rate at which the costs increased is due to that the mix of services consumed changed, rather than that the cost for each service performed decreased. The clearest change that followed the reform was that a larger part of the efforts were targeted to older and sicker elderly, compared with before the reform when younger and healthier elderly were given a larger amount of the services. That the population becomes older and that older people require more care is likely a partial explanation to why the mix of services consumed changed. The demographic changes cannot, however, explain why the change in service pattern happened right at the time of the transfer to the municipalities.

If the two reforms are compared – the transfer to the municipalities of the schools and the Ädelreform – you will find both decisive similarities and differences. Both

took a very long term to process, while at the same time there was a broad consensus among the political decision makers about what needed to be done. If the problem had been merely obtaining support in Parliament, there would have been a majority for the reforms as early as in the early seventies. The government studies that were conducted during the seventies and eighties also recommended going in the direction of transferring authority to the municipalities. The Social Democrat governments that pushed through the reforms could have gathered support from any other party in Parliament with the possible exception of the Center Party ("*Centerpartiet*") for Elder Care, and the Liberal Party ("*Folkpartiet*") for the schools. It should be emphasized, however, that even the opposition parties which would not have supported a deal in Parliament, thought it was necessary to make a change in the responsible entities for these activities. The opposition parties were however critical to the design of the reform proposals.

If a comparison is made between the results of the two reforms, they have in common that the cost trend curves were broken and became flatter in connection with the reforms. The effect was stronger for Elder Care reform than for schools, which can be explained by that the latter was more strictly regulated and that there therefore was less room for local solutions.

It is also possible to compare the two reforms in terms of conflict and activity in different contexts. The two reforms had in common that they created very little involvement among the citizens. The debate was going on in both cases during the election of 1988, but the proposal did not become issues in the election, in spite of the fact that Elder Care issues were pushed hard by the Liberal Party when the election was imminent. Nor was the issue of the responsible entity for Elder Care the subject of much debate in the media. In this respect it strongly differs from the transfer of responsibility for schools, which was preceded by a wide-spread and loud debate in the media. The latter can partially be explained by that the process to some extent happened to coincide with the ongoing salary negotiations and the labor conflict that came as a consequence of this. The issue of teachers' salaries became intimately interwoven with the issue of the responsible entity. Drastically raised teachers' salaries also became a game token in the process of transfer to the municipalities. The Minister of Finance, Kjell-Olof Feldt talked about "lubricant" to induce teachers to go along with the transfer to the municipalities.

The provision of extra government money to make the parties involved accept changes was a distinguishing characteristic for both reforms. The reorganization of the tax structure brought with it a possibility of overcompensating the municipalities for their new responsibilities by means of the municipalities raising taxes more than the counties lowered them in connection with the responsibility for Elder Care being transferred. Additional resources in the form of money from the national government were brought in both in connection with the transfer of responsibility for Elder Care and for schools. It is difficult to explain, using traditional – rational – economic theories, why extra economic compensation was necessary to allow a change. According to those theories, the transfer of responsibility would be almost an issue of book keeping. Trying to justify such transfers with arguments about efficiency seems less meaningful in such a context. If the issue had

been one of book keeping there would also have been no need for a “lubricant” to achieve the decision.

That there was a need for extra funding to induce the involved entities to accept change is, however, consistent with economic-psychological theories. According to e.g. the endowment effect the actors will value something they already have higher than something they do not have (but might get) and therefore demand compensation to make the change, even if that to which they change has the same expected value as that which they give up. Also the fact that the transfer to the municipalities was seen as a way to break old patterns and reorganize the activities from the ground up can be explained by such theories. Change was induced by moving the reference points and the cost structure was reevaluated using new mental accounts after the transfers of responsibility. That there was such a motive is stated by, among others, the then Chairman of the Association of Swedish Municipalities, Lars-Eric Ericsson. These findings hints that politicians are not unaware of how people react in decision situations and that by phrasing the alternatives in different ways it is possible to make decisions easier or harder and that it might be necessary to overcompensate to achieve decisions that comprise change.

Results

In this thesis it have been found that voters will react disproportionately negative to tax increases that are larger than the growth of the economy. On average, the ruling coalition will lose 2.5 percentage points of the voter support in municipal election when taxes are increased faster than economic growth, in many cases enough to lose the election. At the same time, no effect could be observed regarding the tax rate or tax increases in general. It is also observed that voters are short sighted and only react to tax increases that have taken place the year before the election.

It is also shown why political changes could take very long time even when the political decision makers agree about what should be done. In the two cases studied in this thesis there was a majority in the parliament about the necessity of transferring the responsibility to the municipalities for decades, but individual actors were able to delay the process by creating disagreement on how the transfers should be made and when.

The research shows that the one of the most important drivers behind the reforms was the use of extra government funding “lubricant” to silver line the offers. Additionally, in the case of the school reform, the labor market conflict made it possible to connect the decision to the salary increases that the teachers were granted. This made it possible for them to integrate their loss (the change of employers) with their gain (the salary increase).

In the case of the Ädel reform one important factor contributing to the decision was that the Government in the negotiations was able to frame the decision as between two alternatives, both of whom implied change. Thereby, status quo-bias

was avoided. The rapidly escalating costs during the 1980s can probably also have contributed to that the changes were in fact implemented. If the costs had continued to increase at the rate that they did during this period before the reform, the costs by year 2002 would have been close to 50 percent higher than what they in fact were. If the future costs were used as a reference point the alternatives that provided change would look more attractive.

It can also be observed, in both case studies, that the transfers of responsibility led to significant changes in the cost trend curve. This would not have been expected if the transfers meant nothing but another responsible party.

In reality the reforms implied also changes in how the services were provided and – in the case of Elder Care – who would get them. One explanation could here be that the municipalities was not bound by previous decisions and could reorganize the services. One example is that most municipalities got rid of the *Sjukhem* and *Ålderdomshem*

The general conclusion is however, that it is rational for politicians to take economic psychological effects into consideration when they design or react to policy proposals.

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Can Behavioral Economics Improve the Understanding of Politics?

by

Erik Lakomaa

Abstract: Classic Public Choice theory has been very important in explaining various political phenomena. Incorporating insights from behavioral economics could possibly improve the analysis of the shape and function of political institutions.

Even if institutions are fundamental in the analysis of policy-making they are often taken as given. Phenomena from behavioral economics such as self-serving biases, loss aversion, encompassing sentiment coordination, status quo bias, endowment effect and framing should have good potential however provide an explanation for the shape of institutions.

A common result of these phenomena on policy is Path Dependence, which is consistent with institutional theory. In this paper, the foundations of such a behavioral model are outlined and some areas in the domain of tax and welfare policy where the model can be applied are suggested.

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1. Introduction

The classical Public Choice theory¹ has contributed much to improving the understanding of the political process. It has described how, for example, bureaucrats or politicians gain from the government growing in size, and it describes how rent seeking can be the driving force behind the legislative process (Buchanan & Tullock 1962, Tullock 1965, Stigler 1971, Peltzman 1976, Niskanen 1971). Recent advances in behavioral economics² can however add a dimension to the analysis, especially when it comes to the understanding of how the voters' demand for certain policies shapes institutions. Institutions have been part of economic historic analysis ever since the seminal works of Veblen (1899), but the question why institutions look the way they do deserves more attention. In recent years some attempts to merge institutional theory with non-rational theories have been made (North 2005) and this paper is in this tradition.

During the last three decades, a growing number of studies have explored how economic actors are constrained by bounded rationality. How people act under bounded rationality has been thoroughly researched concerning behavior in the financial markets and many of the findings can be applied to other areas as well (Ellsberg 1961, Knetch 1992, Loewenstein & Elster, 1993, Loewenstein, O'Donoghue & Rabin 1999, Odean 1998, Rabin 2000, Shafir, Diamond & Tversky 1997, Thaler 1980, 1994, Strarmer 2000).

The ability to make fast decisions using rules of thumb – heuristics – does not need to be a defect but can be a skill of evolutionary value (Dawkins 1989). During the major part of the history of man, when we lived as hunters and gatherers, the ability to make decisions with limited information by using simple rules of thought was likely to be a skill that increased the chances of survival.³ Because of this, we can expect that humans have a drive to use heuristics in today's modern society as well. Empirics, both historic and from experiments, indicate that this is the case (Cramerer, Loewenstein & Rabin 2004, Schkade & Johnson 1989, Kahneman & Frederick 2002, Kahneman & Tversky 1979, 1984, Knetsch 1989, Loewenstein & Adler 1995). It is reasonable to assume that these effects also could be applied to politics and the study of political institutions and such an overview is provided in this paper.

1 It can be discussed whether the expanded theory where Public Choice is complemented with behavioral economic insights should be seen as a part of the public-choice theory or as a stand-alone theory. This philosophical question about the hierarchy of sciences falls outside the scope of this paper, and I will therefore use the term Public Choice – or classical Public Choice – as something that is separate from the theory that I describe in this paper. If we use Tullock's definition "the scientific analysis of government behaviour" (Tullock, Seldon & 2002, p 3) my analysis, however, is definitely part of the field of Public Choice. The most widely used version of Public Choice is however based on neo-classical assumptions and does not incorporate behavioral effects. This "classic" Public Choice falls clearly outside my field

2 Behavioral economics are also called *economic psychology*. The terms are here used interchangeably.

3 Those who encountered a dangerous animal during their hunt had to make a quick decision, flee or fight? Those who searched for further information or tried to do more advanced risk calculations would quickly be eaten, and their genes would come to an evolutionary dead end

The paper is structured as follows: Section 2 provides a general example of how classic Public Choice could be supplemented by behavioral insights for enhanced understanding. Section 3 explores why we might encounter areas where we have significant disagreement between politicians and voters. Section 4 looks into the kin rhetoric and its effects on policy. Section 5 deals with some of the most used behavioral economic regularities: reference points, status quo biases, and their implications on policy. Section 6 deals with the specific effects on welfare policy. Finally, section 7 deals with Path Dependence, which may be the result of many the abovementioned behavioral regularities.

2. Public Choice and Behavioral Economics

That rent seeking politicians must adapt to the wishes of the electorate is a straightforward assumption. In a democracy, it is the voters who make the final decision about the policies. If there is widespread public resistance against the current policies, the elected officials are voted out of power. Therefore, it is a reasonable assumption that the demand for certain political solutions to some extent determines which policies are implemented. One reason that countries such as Sweden and Norway have extensive public welfare systems while countries like Switzerland, the United States and Japan have low taxes and a high degree of private responsibility for welfare services, could, after all, be that the electorates have different preferences (Alesina, Glaser and Sacerdote 2001).

In many instances, it is not rational for voter to spend much time on evaluating political alternatives. The probability that one's vote will affect the outcome of an election is very slim, and it is therefore not rational to study the political programs in detail or to evaluate what various possible majority coalitions imply. To vote for the same alternative as in the last election, or to vote for the same alternative as your father, can often be a working rule of thumb. However, you can easily observe that people around you have considerably greater interest in and knowledge about politics than Downs' (1957) model of rational ignorance would indicate. People also vote to a greater extent than predicted by this theory. However, it cannot be ruled that using heuristics is an appropriate and widely used model for making decisions. It is reasonable to assume that the same degree of rationality, or lack of rationality, guides you whether you trade financial instruments or act as voter and office holder; we do not become a new type of human beings when we enter the voting booth or enter into the Parliament building.

Another basic assumption in economics is that only revealed preferences are valid (Sagoff 2004). If I buy an orange, it is reasonable to interpret this as if I actually want an orange, and not as if I wanted an apple. Here, I argue, many of the classical public-choice theorists draw a false conclusion when they say that there are fundamental differences between acting within the field of politics and acting within the field of economics.

Few Public Choice researchers would accept the hypothesis that the voters vote for a political party because they approve of the party's policies – that Social Democrats vote for the Social Democratic party simply because they are Social Democrats. This is, however, probably something that most of us – as citizens – would agree with.

In the world of politics, there are a number of phenomena that cannot easily be explained with the aforementioned traditional theories. The purpose of this paper is not to invalidate Public Choice theory, but to describe certain areas where insights from Behavioral Economics can increase the degree of explainability and suggest possible new research areas.

The phenomena, or rather regularities, from Behavioral Economics I will use in this paper are the following:

Status Quo-bias /Endowment effects (Thaler 1980, Knetsch & Sinden 1984 Samuelson & Zeckhauser (1988)

Result: Path Dependence and ratchet effects both when it comes to programs and ideas

Act on perceived rather than actual probabilities (Rabin 2002), law of small numbers (Slovic 2000, Kahneman & Tversky 1971)

Result: Over/underestimation of the risk of having to resort to welfare

Cascades (Kuran 1996, Kuran & Sunstein 1999, Bykhchandani et al 1992) e.g. we tend to do as other people around us do without collecting new information.

Result: Path Dependence and discrepancies between votes and representatives

Self-serving bias (Johnson, Feigenbaum & Weisberg, 1964, Miller & Ross, 1975, Babcock & Loewenstein 1997). Overestimation of the validity of our own position.

Result: Hubris or over/underestimation of risks

Kin rhetoric and “the people’s romance” (Salmon 1998, Klein 1998, Klein 2005)

Result: “Unnecessary” solidarity or bias toward statist position

The implications of these regularities will be dealt with in the respective sections but the reader can already see that Path Dependence is a common factor. Since Nelson & Winter (1982), Dosi (1982) and David (1985), Path Dependence is a central tool of analysis in economics and economic history.

3. When Voters and Politicians Disagree

People have a tendency to evaluate ambiguous information in a way that is in their own interest. They also often take credit for success but deny responsibility for failure, often by blaming external factors. This phenomenon is called *self-serving bias* (Johnson, Feigenbaum & Weisbeg 1964, Miller & Ross, 1975, Babcock & Loewenstein 1997). Political action can be driven by self-serving biases in different ways and can have potential disastrous consequences. When the First World War broke out in August 1914 all the Great Powers; Germany, Russia, Britain, France and the Austro-Hungarian Empire believed that their side would win a quick victory. The breakout of war was even met by large cheering crowds in cities like London and Berlin (Tuchman 1962). Obviously both sides cannot win a war and if the leaders (and the citizens) had a more realistic outlook on the results they may have been more reluctant to enter in the conflict. Self-serving biases could be a reason to why all participants overestimated their abilities.

Self-serving biases help to increase the understanding not only of big and unsettling events such as wars but also of more mundane decisions. In combinations with *cascades* (see below), self-serving bias can contribute to a considerable gap between the policies that the political parties represent and the policies that the voters want (Kuran 1995). In most democratic countries, there are central issues where there is a deep divide between the majority of the voters and the majority of the representatives in the parliament. With a political system that allows free entry, you could assume that if the existing political parties did not match the voters' view on one issue, there would be a new party that shared the views of the existing parties, but with a revised view on the dividing issue. However, this is not how it works. The politicians have created entry barriers in the form of regulations for party financing, percentage thresholds and government contributions to the established parties. Despite these obstacles, you might expect that there would be no systematic differences in opinion between the electorate and the elected. However, self-serving biases and cascade theory could explain why such differences emerge and are reproduced. The politicians may simply believe that their views are shared by the people – because their views are the correct views. It is reasonable to assume that this is a process within the political institutions since it would be very difficult, if not impossible, to calculate which parties that would benefit from the long-term effects of certain welfare programs. There are just too many factors to consider – demography, economic development, international relations and changes in preferences to mention a few – for it to be meaningful to try to determine voter movements in the decades to come.

This can be compared to an experiment in which test persons were to guess the outcome of a trial. Those who got the task to analyze the outcome from the defendant's perspective gave one answer, and those who got the task to analyze it from the plaintiff's perspective gave another. This happened in spite of them getting the same information (Babcock & Loewenstein 1997). Also in this experiment, it appeared as if the test persons assumed that the side that they represented was right. One can note that when politicians, or other elite groups, for instance realize that people don't share their views, they sometimes claim that people are

victims of false consciousness or guided by “invisible structures”. In this case, there is no intention to force an unpopular view onto the voters. Instead, the policies are directed by a genuine belief that they are executing the will of the people (Payne 1991) writes:

Everyone wants to have a high opinion of himself [...] When the congressman comes to Washington, he is surrounded by beneficiaries and claimants who are pleading for his ‘help’. He is strongly invited to accept the role of philanthropist, strongly encouraged to believe that he has assisted people and left the country better off by funding government programs [...] This high self-opinion would be directly threatened if the donor of the funds [that is, the taxpayers] were brought into the picture. As soon as one recognizes that in order to help some people you have to hurt others, much of the glow goes out of being a congressman. For this reason, congressmen are reluctant to face the opportunity-cost issue⁴.

These internal political processes can be explained with cascades (Kuran 1996, Kuran & Sunstein 1999, Bykhchandani et al 1992). If everyone around you shares the same opinion, it is rational to assume that this opinion – or the perception of reality supporting it – is correct. To spend time gathering and processing information that could disprove your views is then irrational, because the probability is high that you would reach the same conclusion as the prevailing one.

These effects can be fortified by a deeper divide between the electorate and the elected. If the political units are small and decentralized, those elected will often meet the voters – at the supermarket or at social events. This enables politicians to discuss proposals and to get ideas for new ones. Maybe more importantly, they meet the people who are affected from their policies (Slovic 2000). A centralized political system with a limited political class would, according to this theory, produce more policies that clash with the views of the voters than would be the case in more decentralized systems.⁵ The outcomes of referenda can be used to test this theory. In countries where politicians initiate referenda, such as Sweden, one could safely assume that a referendum would be initiated if, and only if, the political majority is convinced that the alternative that they advocate would win. In political systems where the people through citizen initiatives can force referenda – usually by collecting a certain number of signatures – as in Switzerland or in many American states, or in systems where referenda are mandatory to make some types of decisions, as in Ireland, you cannot expect that a certain outcome is more common than any other. If any side was more likely to win, it would be the side that forced the referendum. The required number of signatures is seldom comparable to the number of voters. However, one can assume that since it takes a lot of resources to collect the signatures, people abstain from undertaking such projects when the perceived chance of winning the referendum is slim. If the abovementioned theory is correct we would find that the initiator’s side often loses referenda.⁶

4 Payne 1991 p 47

5 For an overview, see Mueller 2003, pp. 209-229

6 In Sweden, this appears to be the case. Out of the six referenda held after the adoption of universal suffrage the initiator (the Government side) lost 3 (Alcohol Prohibition 1922, Changing from left- to right-hand traffic 1955, Joining the Economic and Monetary Union of the European Union 2003), won 1 (Joining the European Union 1994) with two ambiguous cases (Tax Funded Pension System 1957, and Reliance on Nuclear power 1980) were no alterna-

The way that the political process works on a personal level can also have large effects. The personal cost of opposing a proposal that is supported by the other members of a political assembly can therefore be greater than the cost of opposing a proposal that is supported by citizens that you never meet. This would imply that larger political units are less likely to make decisions that reflect the wishes of the voters. Arthur Montgomery argued that the most important institutional change in Sweden since the land consolidation reforms (mostly done in the 18th century) was the municipality mergers in the 1950s and 1960s⁷ On this point, he got support from Myrdal (1982), who especially emphasized the increased gap between the electorate and the elected, and the loss of the social control:

The distance, both in geographical and human terms, to those in power has increased enormously. These are no longer neighbours who know each other, live close to each other and close to the rest of the locals, and who are subordinated to the social control imposed by the local society [...] Small-scale solutions meant that we [when Myrdal was the mayor of Mariefred⁸] constantly met in the streets, at home and at the local restaurant. This led to a local interest in what I did and to neighbor control.⁹

This development contrasts with the situation in places where a very decentralized decision making process has prevailed. In the Swiss canton Appenzell, voters meet on the square to make collective decisions. This leads to some interesting results for the political decision making. Taxes have, for example, only been raised slightly since the end of the 19th century. This has resulted in the social services being rather rudimentary. A conclusion to be drawn from this is that it seems to be more difficult to introduce taxation of others (few would vote for taxes that affected themselves negatively) if those who will pay the taxes stand next to you when the decision is made.¹⁰ The costs of the decision-making will be weighed against the costs of the policies. Depending on your political views, you can also add negative effects which follow when the policies in demand have not been produced. But that is a natural consequence of democracy. This area deserves to be explored further in future research.

tive reached a majority.

7 Here we can note that the municipality reform was introduced in part because the merged municipalities were considered necessary to deal with all the different programs that were needed in the new comprehensive school system. Small municipalities were not thought to be able to offer a sufficient number of study programs. When the reform was done, however, the different study programs in the unified school system were almost gone, but the reform was irreversible (Myrdal 1982 p 89). On this account Myrdal speaks about the latter of the two waves of municipality mergers and Montgomery about the first.

8 Myrdal was appointed, not elected, but obviously considered the residents of Mariefred his constituency.

9 Myrdal 1982 p 86

10 The same result could however also be a result of cascades

4. Kin Rhetoric

To talk about the society as a family or about the leader as a father is classical political rhetoric. “The People’s Home”¹¹, “the Fatherland”, “Uncle Sam” etc, have often been invoked to motivate various kinds of government projects. Salmon (1998) argues that the artificial or metaphorical use of “*kin rhetoric*” is designed to exploit the natural solidarity between relatives. “*We address non-relatives by kin terms when we are attempting to promote solidarity and solicit aid*”¹² This could be combined with the habit of looking at the government as a fatherly figure. Klein (1998) gives an explanation for how this can work:

Relationships in the household are communal and altruistic. Especially for the formative period prior to puberty, the child is reared obeying a supreme central authority that and overrides her own judgment and coordinates activities in a top-down fashion. [...] The family is the cradle of encompassing sentiment coordination. It is plausible that the individual’s thought patterns would follow that mental model in dealing with other social issues.¹³

There is strong evolutionary evidence for this theory. Since we have lived in groups where we have been relatively closely related to each other during the major part of our history, it has been a recipe for evolutionary success to help those surrounding us, but not to help those to whom we are more distantly related. This phenomenon is found among many species (see Daly & Wilson 1978 for an overview).

Salmon (1998) argues that the reasons for the success with political “kin rhetoric” are natural and based on the fact that we experience ties to relatives early in life, while friendship and reciprocity is experienced far later. This makes references to the former more powerful.

We do not need to be related to be affected by the kin references. Altruistic behavior toward relatives is not sparked by the kin relationship as such (which is often difficult to ascertain), but by factors that are or have been closely correlated to kin relationships (Salmon 1998, Stack 1974). Johnson et al (1985) have in experiments showed that references to kin relationships (ex. “fraternity”, “brotherhood”, “soul sisters”) in political speeches stir up a more positive response from the audience (the readers in this experiment) than the use of other words such as “neighbors” or “citizens”. The result of the experiment goes well with less systematic observations of the political reality. “*The fact that politicians and union leaders persist in using kin terminology suggests that it is an effective strategy for arousing the emotions of an audience.*”¹⁴

A number of studies show that we tend to view persons who are similar to ourselves as “relatives”. This is true both for similar looks and similar behavior (Burch & Gallup 2000; Lieberman et al 2003, Shepher, 1971, Platek et al 2002), and we tend to view these persons in a more positive light than others (Byrne et all 1971,

11 Swedish “*Folkhemmet*”

12 Salmon 1998 p 47

13 Klein 2005 p 21

14 Salmon 1998 p 45

Chen & Kendrick, 2002, Batson et al 1981). References to similarity should therefore be effective in political rhetoric (Park & Schaller 2005).

Klein (2005) has also described a closely related phenomenon that he calls encompassing sentiment coordination¹⁵, which states that agents are rewarded if they embrace the same idea as others. He gives evolutionary support also for this theory. Klein continues:

Millions of years of primate evolution and more than one million years of human evolution in hunter-gatherer bands of fifty to one hundred people might well have selected for [this]. Major group experiences were encompassing.¹⁶

According to this theory it is rewarding to go with the flow or follow momentum and also explain (irrational) support for Government or nationalism, as in “*my country – right or wrong*” which in turn could lead to excess support for collectivist policies.¹⁷ This, too, is an area that deserves to be the object of future research.

15 Klein 2005 p 11

16 Klein 2005 p 21

17 Klein 2005 p 21 also states that the Leader (and his opinion) could be the reference point when different alternatives are evaluated. See also McClosky 2000 p 185

5. Path Dependence and Behavioral Economics

One of the most important theories in economic history is *path dependence* (David 1985, 2000). However, it is also possible to apply this theory on ideas. If you have advocated an idea for a long period of time – it could be a religious idea or a political one – it is often difficult to give it up. This could also be viewed analogously with the endowment effect (see section 6) that has been observed in experiments (Kahneman & Thaler 1987, 1990). This is partly a traditional exit cost. Changing one's mind may cause reputational effects, but just as we can observe in other situations, people seldom consider such costs. In this case, we can assume that the costs primarily are lost credibility and prestige. Someone who has argued that the dividing line between “generous welfare programs” and “ruined welfare” goes at 90 percent compensation for sick leave and unemployment compensation will have a hard time accepting policies that lead to lower levels of compensation. The endowment effect can, however, add to the exit cost and make it harder to abandon ideas that are no longer viable.

One could also imagine that there are network externalities (David 1985) that make it difficult to change decisions made earlier. This is something that Myrdal (1982) observes when he studied big municipalities:

Social developments are usually not reversible. Questions about taxes and debts are as difficult as in every divorce. Great buildings have often been built for the municipality's administration, usually in the central community. At a division of a municipality, they were too big for the part of the municipality in which they were included, and too inconveniently located for other part.¹⁸

Because of earlier policies, a reversal to the previous order is considered too costly and despite the possibility of fundamental changes, investments already made block an adjustment of the policies to the new situation. One can assume that individuals work in a similar way. When a political program has been introduced (whether it is a tax regulation or a system for social benefits), those who are included in the system adapt to the new situation.

Housing subsidies and interest regulation induced families to buying houses to a greater extent than they otherwise would have been likely to do (Borg 2004). A change would not be perceived as something positive by these families, and it would probably be opposed or voted against. Voters are affected by the so called sunk cost fallacy; they fail to see it as a sunk cost and act accordingly. This will create Path Dependence. But this Path Dependence could also be on a non-monetary kind – that they have invested intellectual capital into defending a previous monetary act – and therefore are ‘obliged’ to stick with it. The same phenomenon could possibly be behind the difficulties to reform the pension system. In this case, the issue is complicated by the fact that it is so politically charged due to its being described as the *Jewel in the Crown of the Welfare State*.¹⁹ In order for the pension reform to be implemented, it had to be framed as a small change to the existing

¹⁸ Myrdal 1982 p 89

¹⁹ Lundberg 2003

system, even though the reform had to do with fundamental principles behind the system. To reach acceptance for the pension reforms, long periods to phase out the old system have been necessary.²⁰ The result has been that those who were old enough to vote about ATP, the national supplemental pension scheme, in 1957 were allowed to stay in the old system with guaranteed pensions while those who are younger, to a varied extent, are subjected to the new conditions.

²⁰ See e.g. Borg 2004 p 206ff

6. Effects on Welfare Policy

It is also possible to find applications for Behavioral Economics, which potentially may improve the analysis compared to traditional Public Choice, in the field of welfare policy. I will here discuss a few applications that relate to the demand for welfare programs. This should be seen as an opposite to supply models in the field of welfare policy where the programs are created to provide bureaucrats with power or resources, or to demand models based on the assumption that voters through manipulations by those in power have been led into a state of government dependency that they cannot break free from.

Experiments have shown that we often overestimate the risk for extremely unlikely events (Slovic 2000). One explanation for the great demand for welfare services could be that the citizens underestimate the chances of success and overestimate the risk of ending up at the bottom of society. This could lead to welfare addiction, but those who estimate the risks differently could at the same time be against the welfare programs. How you estimate the risks could in turn be related to historical and institutional factors, which could explain that there are often big differences in the welfare politics in different countries. The law of small numbers (i.e. that we tend to overestimate the probability of very rare events) can in this instance give two diametrically different outcomes depending on which institutions it is combined with. These kinds of explanations constitute one of the strengths of the Behavioral Economics. Someone who believes that there is a great risk of being killed in an airplane crash or by the side effects of a medicine will be prepared to make big investments to reduce these risks. At a personal level, it can mean avoiding air travel or avoiding medicines that you believe are dangerous. This behavior brings personal costs with it. In the voting booth, however, is it much cheaper to embrace these kinds of principles for minimizing risks, and we get an integration of rent seeking and psychological demand factors affecting the decision. A result of this would be that voters are stimulated to vote for things that have low private costs but possibly considerable negative effects on society. Extensive research related to results has been conducted (Libecap & Wiggins 1984, Keser & Gardner 1999), but note that the cause could possibly be found in Behavioral Economics. This is another example of how understanding of political action can be improved by including these models.

7. Reference Points, Loss Aversion and Ratchet Effects

The view that advocating big changes – except in very special circumstances – is not a feasible strategy for winning elections is a not very controversial.²¹ Through small changes, you can move society in a direction that you desire without confronting too much opposition. When a subsidy or taxation base is established, it will be taken for granted and becomes a constant. This is compatible with the theories about status-quo effects, but the theory says nothing about what the politics will look like in practice.

Another common phenomenon related to this is the ratchet effect, which makes the direction of the decisions more important than the level in absolute terms, often combined with the fact that it is easier to introduce laws, subsidies, regulations or taxes than to abolish them. This is expected to lead to an ever increasing quantity of legislation since what already exists will be taken for granted. Thereby, politics works like a ratchet that can only turn in one direction. Hence, political battles will essentially always be fought between those who want to introduce new regulations and those who want to preserve status quo (Kingdon 1995). It is seldom the case that two proposals for change stand against each other. Politicians often think in these terms, and a complete ideological school, the reform socialism or the *Fabianism*, which often dominates the Social Democratic movements, is in principle based on these ideas even if this area of research emerged in recent years. That these ideas are significant, you can tell from what those in power say. In an interview with Swedish Prime Minister Göran Persson, Peter Bratt summarizes Perssons views:

It is a way to transfer parts of the economic growth to the general welfare system without making it noticeable. The wage earners get a part of the standard improvement and give up the rest to the welfare system [...] There is a big difference between paying more of what you already have and getting less of what you don't yet have. That is how it has been done ever since the war. From 1950 to 2002, private consumption increased with 127 percent. During the same period of time, the public consumption increased with 274 percent. The growth was enough for both of these things. During this period, the tax rate, or the tax quota, that is the part of GDP that was paid to the government in taxes, increased from 20.5 to 51.8 percent.²²

The public-choice explanation of the ratchet effects is that each time that politicians introduce a new law, regulation, or subsidy, they create a group – sometimes a group of citizens but usually a group of politicians and government employees – that benefits from this measure. A new regulation must, for instance, be followed by one or several government employees – people who will have reasons to obstruct if the program is abolished. As Olson (1962) shows, small and well organized groups often have advantages over larger but unorganized groups. In addition to the fundamental efforts to explain the great expansion of visible ratchet effects, insights within the field of Behavioral Economics can contribute with explanatory factors that don't originate only from the bureaucrats affected by the measures

²¹ A contrast to this is Higgs (1987) model about crises as a driving force for expansions. But this is less clear when we as Kingdon (1995) separate agendas from alternatives.

²² Bratt, 2004 also see Rodriguez 1981

but also from the public (that is the clients/buyers). The strength of the argument increases if factors that affect the demand are included in the analysis. These factors can contribute to the phenomenon, and originate from both bureaucrats and voters (as consumers of public goods).

Instead of starting from scratch with new legislation, politicians take the existing legislation for granted and make small, gradual changes. By using that method, they don't have to create extensive systems of far-reaching changes. They don't have to formulate the goals – they are given – and the changes that they propose are perceived as feasible (Kingdon 1995). A political program that has been established is seldom fundamentally questioned, it is surrounded by low levels of uncertainty and the changes tend to be made in steps.

An example of how fast such a process can go is the Swedish *Högerpartiet's* (the Conservatives) quick acceptance of the ATP-system (Borg 2004, Edebalk, 1996, Molin 1965). Even though they strongly opposed a mandatory national supplementary pension scheme as late as 1959, they proposed that the system should be expanded in their 1962 election platform.²³

Even if the acceptance of new programs is often a quick process, the introduction can take a long time. Borg (2004) shows for example that the 1994 pension reform was preceded by 10 years of studies and the introduction in 1913 of *folkpensionen*, the universal basic pension system, was preceded by 36 years of studies.

Incrementalism can also be used as a method by those who want to manipulate the political process and its outcome. People are often unwilling to take big steps at once. When the decisions are made gradually, it is also more difficult to see what the final result will be. For these two reasons, those who advocate radical change often have to push for small parts of the change, one at a time. Once a program has been introduced, it becomes easy to expand it, new groups can be included, the requirements can be changed, etc. The trick is to get a foot in the door. The difference between agendas and alternatives is that changes of the agenda occur in big jumps and not step by step. The creation of alternatives, on the other hand, is a step-by-step process. When those in power see which alternatives they have, they choose the ones that they already know of and that go hand in hand with their ideology. The agenda, however, can change quickly, for instance through an election or an economic crisis (Kingdon 1995, also see Higgs 1987). It is often more difficult to oppose a proposal if you don't view status quo as the alternative. If you don't do that, you have to formulate a complete alternative that cannot be objected to, and you also have to define your premises and explain what the goal is.

Loss aversion can also explain macroeconomic phenomena such as (downwardly) rigid (nominal) wages.²⁴ Behavioral Economics may give a better explanation in this instance. Since the economic agents are loss averse and guided by a

23 One cannot say that they simply adjusted themselves to the result of the referendum since the referendum did not give a clear majority in favor of any of the three alternatives. Instead, the issue was settled in Parliament, where the support from a member of *Folkpartiet* (the Liberal party) was needed to push through the government's proposal

24 This is a common assumption in economics and the explanation is often thought to be so called *menu costs* (Romer, 2001).

status-quo bias, a cut in the real wage that is caused by a cut in the nominal wage is perceived as worse than a cut in the real wage that is caused by a decreased value of money.

Experiments conducted by Kahneman, Knetsch and Thaler (1986) confirm this thesis. They found that the acceptance of a wage cut in a zero-inflation economy was smaller than the acceptance of no wage raise in an economy with high inflation, even if the outcome in real terms was the same. The concept of money illusion is important in Keynesian economics. It says that economic agents make their decisions based on nominal rather than real income, a theory supported by behavioral economists. Baker, Gibbs, and Holmström. (1994) and Shafir, Diamond and Tversky (1997) have shown that employees accept real-wage cuts as long as the nominal wage is not cut. Also in this case, the major part of the research has dealt with phenomena in the financial markets. A classical example (Odean 1998) that is usually used to illustrate the loss aversion is the following: You have two shares on the stock market, one that has increased in value and one that has decreased in value. You have to sell one of them to repay a debt. Which one do you sell? Many people answer that they would sell the share that has increased in value even though – at least in a world with capital-gain taxes – is more beneficial to sell the one that has decreased in value.

The same effect is found in the real estate market. Genegove and Mayer (2001) have shown that the advertised prices of apartments in Boston are strongly linked to the prices that the apartments were bought for. According to neoclassical theory, the apartment seller should view the price that he or she has paid as a sunk cost and not let it affect the selling price. But since people hate to sell things and make a (nominal) loss, the buying price matters.

The behavioral economic theory that is most widely known among laymen is the phenomenon that makes people demand much more to sell a good that they own than they would be willing to pay to acquire it. Thaler (1980) named this phenomenon endowment effect. In a classical experiment, Thaler (1980) provided half of the test persons with a coffee mug. They were then asked at what price that they would be prepared to sell the mug. The half of the group that was not given a mug was asked what they would be willing to pay for a mug. According to neoclassical theory, there should be no difference between these buying and selling prices. However, in the experiment, the selling price was far greater than the buying price. The explanation is said to be that those who got a mug saw it as theirs and were reluctant to give it up while those who got no mug saw the mugs as just any mugs. Goods owned are apparently valued more highly than identical goods not owned. The non-owner's potential gain from acquisition was apparently smaller than the owner's potential loss from sale. The effect has since been widely replicated, (see e.g. Kahneman, Knetsch, & Thaler, 1990; Kahneman, Knetsch, & Thaler, 1991)

Samuelson and Zeckhauser (1988) called a similar phenomenon the status-quo bias – this phenomenon had to do with the unwillingness both to sell and to buy anything. The asymmetry is, just like the endowment effect, a result loss aversion, which in turn is a implication of of prospect theory and reference points (Kahneman & Tversky, 1979).

Experiments conducted by Loewenstein and Kahneman (1991) show that the endowment effect is not sparked by someone receiving a gift,²⁵ but only from the "pain" that arises when people have to give up something that they have. Do agents consider the endowment effect – do they expect that it will affect them? Loewenstein & Adler (1995) find no support for that hypothesis. However, Novemsky and Kahneman (2005), expect that there are situations in which the agents do this: "*There are some cases in which no endowment effect would be expected, such as when goods are purchased for resale rather than for utilization*"²⁶. This has been confirmed by List (2003). In addition to this, Strahilevitz and Loewenstein (1998) has shown that the intensity of the endowment effect depends on how long the item had been owned, whether it had been lost before, for how long it was gone and for how long it had been owned when it was lost. A test of the status-quo effect was conducted by Hartman, Doane and Woo (1991) and dealt with electricity customers in California. The customers were asked how they viewed different combinations of service and prices where one of the combinations was status quo. Regardless of whether it was a combination of a low price and little service or of a high price and lots of service that was described as status quo, most people chose that alternative (also see Kahneman, Knetsch, & Thaler, 1991). We should be able to observe the same effect when it comes to people's view of the pension system or the health insurance system.

25 Gift giving is however an area that might be explored as a field where behavioral economics can provide new insights in welfare policy

26 Kahneman, Knetsch & Thaler 1990 p 1328

8. Going Further

In this paper, I have pointed out areas where insights from e.g. Kahneman, Tversky and Slovic may have good potential to be used to improve the analysis of political decision-making and design of different political programs, primarily relating to taxes and welfare. The contemporary analysis of political decision-making that the Public Choice school has created has meant a lot for increasing the understanding of these areas. The economic-historical institutional analysis is also valuable in these efforts. How institutions originate and change in different societies and at different times gives us insights about which factors drive the development. Also the theories from economic history about path dependency and network externalities are powerful tools. There are, however, room for new tools derived from non-traditional theories. By adding a demand model and trying to analyze which demand for different types of political services that can be related to the regularities that economic-psychologists had found, the analysis can be made more complete.

If we add the behavioral insights to the classical Public Choice models we are likely to be able to see more rigidity on the political market than with Public Choice theory alone, because not only the rent seeking effects but also mental effects may create Path Dependencies. This supplement also has the potential to explain why these rigidities take the shape they do.

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Are you better off Now than you were Four Years Ago?

Psychological Insights in Tax Policy and Voter Behavior

Erik Lakomaa

Abstract: According to a hypothesis derived from *prospect theory*, the cognitive bias of *loss aversion* would make voters more likely to punish the governing majority if taxes are increased faster than the growth of the economy, i.e. if they are worse off in absolute terms. This hypothesis was examined using panel data regressions on data from a new and extensive database over Swedish municipal elections, and tax rates, from 1976 to 2002. It was found that a governing majority loses on average 2.5 percentage points of voter support if such tax hikes take place. At the same time, the unemployment rate, the inflation rate, the tax rate or smaller tax hikes, did not have any significant impact on voter behavior. This lends support to the assumptions that *small* tax hikes are “free” in terms of voter support and might explain why the high-tax welfare state has been possible and provides an example of an area where insights from Economic Psychology supplement traditional Public Choice theory.

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1. Introduction

In the 1980 presidential election campaign Republican candidate Ronald Reagan asked voters if the four years with President Carter had made them better off. The rationale was that if their answer was ‘no’, they should vote for change. Even though Reagan’s one-liner was new and striking, the idea behind it was not.

Politicians have long been aware that voters tend to punish incumbents when the economy falters¹. The assumption behind Reagan’s question is that voters, like in the classic Public Choice setting, act as any economic agents. The effect of economic factors on voting behavior has been studied by a number of researchers but the main focus has been on macroeconomic factors. The first attempts to find a quantitative relationship between economic development and election outcomes were made as early as in the 1930s (Tibbits 1931). That economic performance influence voter behavior is fairly uncontroversial in modern economics. Bengtsson (2002) writes: *“Few social scientists question the general theoretical idea that economic factors influence the voter’s evaluation of the government”*². Economic voting is one of the theoretical foundations in this paper.

The other theoretical foundation in this paper is economic psychology, especially the concept of loss aversion and reference points which will be discussed later on. In this paper the growth of the Swedish welfare system will be analyzed through these frameworks. As in most countries in the Western world, the public sector of the economy in Sweden has increased greatly – both when it comes to absolute and relative expenditure and e.g. number of people employed. The last half-century in Sweden is, however, special in many ways. Not only is the public sector larger than in any other democratic nation, but the people seem to like it and has continued to repeatedly vote for parties supporting such a large public sector.

A traditional Public Choice theoretical approach thereby becomes clearly insufficient. The Public Choice model, with a supply model where the growth of the public sector is explained by the work of politicians and bureaucrats who, often contrary to the will of the people, expand the size and scope of government, is in apparent need to be complemented with a demand model where voters’ demands for political solutions are incorporated.³ Adding perspectives from economic psychology – especially loss aversion – might be such a remedy. Therefore an economic-psychological framework will be used in this paper in order to explain one aspect of the development of the Swedish welfare state focusing on municipal elections.

The paper is structured as follows: Section 2 provides a general overview of previous research in economic voting. This is followed in section 3 by a description of the economic-psychological theories of loss aversion and reference points,

1 Se e.g. Pacek and Radcliffe 1995

2 Bengtsson 2002 p 1 Author’s translation

3 Niskanen 2004 notes that the optimum tax level – calculated from a Public Choice perspective where the rationale for taxes is to maximize revenue (which can be used to finance government services or hand outs) while minimizing discontent, – is far lower than the actual tax levels in countries such as Sweden.

together with some implications on policy making that stems from these theories. Section 4 covers misery indices which is a tool that has been used to predict election outcomes. Section 5 describes the hypothesis that will be tested together with a description of the data used to test it. In section 6 the results of the regression is presented. The final section, 7, consists of a summary of the paper and a general discussion.

2. Economic voting

Researchers, e.g. Nannestad and Paldam, (1994) argue that macroeconomic factors can explain about one third of the variation in voter support for the national government. Inflation and unemployment are the most important factors.⁴ These are also the factors that we usually find in *miser*y indices.⁵

That voters are affected by [macroeconomic factors] is not very surprising because they tend to influence our daily life. Further, to understand how unemployment and inflation could affect the personal or national economy requires no advanced knowledge in economics.⁶

Some researchers, however, have opposing views (Stigler 1973, Lewis-Beck 1991) and claim that macroeconomic factors do not affect voter behavior, even though microeconomic factors might. In most cases changes in macro variables have an impact on micro variables, e.g. changes in the inflation rate, unemployment rate or economic growth will also affect the likelihood of having a good job, a good salary and access to cheap consumer goods. It could also be argued that macro variables are good proxies for micro variables and vice versa. When it comes to economic voting on the micro level the support is weaker, as shown by Jordahl (2002). Voters' interest in the economic performance of the government, on local or national level, is however clear; the difficulty emerges when you try to isolate effects of "pocketbook issues". That voters would, in most cases, prefer a government that – other factors, e.g. ideology, considered – could be expected to produce a decrease in inflation, unemployment and taxes (and an increase in government services) is a reasonable assumption.

Another effect that is believed to affect the support for government is "*incumbency bias*", also known as the "*cost of ruling*" (Ström 1990), which implies that being in power costs votes, or that a certain proportion of the voters always vote for change no matter the policies of the incumbent. Paldam and Scott (1995) found that the incumbency bias is on average minus 1.65 percent. It could however be argued that the cost of ruling to some extent can be compensated for by assuming that politicians in power can use the government to finance their campaigns or to erect barriers to entry, such as public party financing, thresholds for representation etc. With perfectly rational voters it is hard to explain incumbency biases since politicians then ought to do what the voters have voted for. However, incumbency bias can be observed in most countries and with that taken into account the uniquely long history of Social Democrat government in Sweden – they have been in power 65 out of the last 75 years – must be regarded as very special.

To sum up, the research mentioned above has shown that voters generally punish politicians who have been in power during economic declines, but seldom

4 Nannestad & Paldam, 1994 p 216, 225, 237

5 The usual explanation for why voters react to changes in these indicators is that they have an unambiguous effect and are widely published. Together with the growth in GDP, the inflation and unemployment rate are the economic variables that most people can be assumed to be familiar with.

6 Bengtsson 2002, p 3

reward politicians who have governed during economic booms. This might imply that voters are aware that politicians have limited (or no) ability to create wealth, but that their ability to destroy wealth is significant. For example, voters act as they assume that politics is a zero- or negative sum game.⁷ It should be noted that some researchers, e.g. Lewis-Beck (1991) and Nannestad and Paldam (1994), have found results contradictory to this theory. They argue that voters experiencing an improving economy are as likely to reward the parties in power as voters experiencing a declining economy are to punish the government.⁸

Some regularities in the field of political economy that have generated much interest from researchers are methods used by politicians to manipulate the economy in order to get re-elected. This is often assumed to be done by increasing spending and cutting taxation before an election, as well as cutting spending and increasing taxation when securely re-elected (see Lindbeck 1976, Mankiw 2000; Alesina, Roubini & Cohen 1997). The result is the so called political business cycle (Mueller, 2004). The opportunistic behavior observed among politicians in some countries (see e.g. Barro 2002, Mueller, 2004) is less obvious in Sweden. Although politicians of various party affiliations to a great extent have tried to woo voters with handouts, attempts to woo voters with tax cuts have been rare. On occasion, politicians in Sweden even have promised higher taxes if elected, like in the national elections of 1982 and 1994. It might be the case that tax increases are of minor concern as long as voters are left with more money in their pocket books than the year before. There is also empirical support that this regularity has been used by politicians. In an interview with then Prime Minister Göran Persson for Dagens Nyheter, Peter Bratt summarizes:

This is a way of transferring parts of the economic growth to the general welfare without the public really noticing. The wage earners get a part of the economic growth and give the rest to the welfare system. [...] There is a huge difference between paying more out of what you have and getting a little less out of what you have yet to get. This is what has happened ever since the war. From 1950 to 2002, private consumption increased 127 per cent. During the same period public consumption (the majority to general welfare) increased 274 per cent. The economic growth was sufficient for both. During this period the tax rate, or the tax ratio, i.e. the share of taxes out of GDP, increased from 20.5 to 51.8 per cent.⁹

7 To what extent voters are aware of this is something that would be very interesting to research. It should be noted that redistribution in many cases can be very costly. The welfare loss (transaction cost) of redistribution could be as large as nine times the value of the hand-out, Browning (1987, 1989). Whether politics is a positive or negative (or zero) sum game, i.e. a process of cooperation or conflict - is a classic rift. Buchanan & Tullock (1962) and Wicksell (1987) are supporters of the first view and Riker (1962) the latter. The theory of Wicksell and Buchanan/Tullock rests on the assumption of the creation of the state by means of a civil contract - an assumption that has been subject to much debate for centuries. My view is closer to Riker's and it is hard to find anybody who claims to have signed a civil contract. But even if you could observe a high degree of cooperation/consensus among politicians this would not rule out the possibility of a conflict dimension between voters and politicians. The question is whether this has been the case in post-war Sweden.

8 In this paper the assumption of backward looking voters (Riker, 1962) are used. This means that voters are assumed to punish failed office holders by voting them out of office rather than to reward candidates for promises given.

9 Bratt 2004

If the assumption that Bratt assigns to Persson is correct we have a strong indication that politicians act according to economic-psychological theory. The political strategy behind the Swedish welfare state can then be summarized into: Split the economic growth into two streams, one to the public sector, one to the citizens in the form of increasing real wages. As long as the real wages do not decrease, voters can be counted on to support the ruling government.

3. The Theory of Loss Aversion

The political strategy described above is exactly what the cognitive bias of *loss aversion* encompassed in prospect theory would imply. Such phenomena are cornerstones in economic psychology, a field of research which receives increasing attention in economic analysis. It was first proposed by Adam Smith (1776) but found its way into modern economics by Kahneman and Tversky (1979) within the framework of prospect theory. It was later also defined for choice under certainty by Tversky and Kahneman (Tversky and Kahneman 1991, Tversky 1992). The popularity of the theory of loss aversion is due to the fact that it can explain many phenomena which remain paradoxes in traditional decision making theory. Well-known examples are the endowment effect (Thaler 1980), the equity premium puzzle (Benartzi & Thaler, 1995), and the status quo bias (Samuelson & Zeckhauser, 1988). A further important aspect of loss aversion is the fact that it can resolve the criticism on expected utility put forward by Rabin (2000) and Rabin & Thaler (2001). They showed that reasonable degrees of risk aversion for small and moderate stakes imply unreasonably high degrees of risk aversion for large stakes. In recent years loss aversion has also frequently been applied in behavioral finance (cf. Barberis et al. 2001, Barberis & Huang 2001, Berkelaar & Kouwenberg, 2000). Kahneman and Tversky's (1979) view of loss aversion is as follows: An individual is loss averse if she or he dislikes symmetric 50-50 bets and, moreover, the aversiveness to such bets increases with the absolute size of the stakes. Kahneman and Tversky (1979) showed that this definition of loss aversion is, in the framework of prospect theory, equivalent to a utility function which is steeper for losses than for gains. (see also Wahlund 1989, Tversky and Kahneman, 1992, Wakker and Tversky, 1993, Starmer, 2000).

3.1 Applications of Loss Aversion

Loss aversion is used to explain macroeconomic phenomena such as sticky wages and prices. The general explanation is so called "menu costs" (Davis & Hamilton 2004). Behavioral economics may however provide further insights; actors governed by loss aversion and status quo bias will perceive a decline in real wages that is the result of a cut in nominal wages as worse than a decline in real wages resulting from rising prices (for the opposite view see Blinder & al, 1998). Experiments conducted by Kahneman, Knetsch and Thaler (1986) support this hypothesis. They have found that the probability of accepting a wage cut in a zero-inflation economy was lower than the probability of accepting the same wage as before in a high inflation economy – even though the resulting real wage was the same in both settings. Money illusion, that actors make decisions based on nominal, not real terms – a cornerstone in Keynesian economics – has also found support among behavioral economists. Baker, Gibbs and Holmström (1994) and Shafir, Diamond and Tversky (1997) have shown that employees will accept declining real wages as long as their nominal wages remain uncut. Wahlund (1989) found a similar reaction when he studied the attitude to tax evasion. Respondents were more inclined to cheat in their tax returns if they believed that taxes had been increased.

If people are loss averse when acting in financial or product markets or in experiments done in laboratories, they might also be loss averse as political agents and it is therefore justified to expect them to react in similar ways to changes in taxes. We can also expect politicians to take advantage of this effect in the same way that they have taken advantage of other effects of tax illusion, i.e. that taxes are hidden from the tax payers, e.g. by using indirect taxation or naming taxes “fees” (see e.g. Sanadajj & Wallace 2003).

3.2 The Effects of Loss Aversion in Politics

Loss aversion in politics has a number of implications, among them that voters would react differently to different kinds of tax increases. In tax policy one might assume that the dissatisfaction caused by tax hikes will be (much) larger if (i) taxes *ceteris paribus* are increased so much that the disposable income of the voter is reduced, compared to if (ii) the tax increase is less than the growth in wages or in GDP. Therefore, the costs of taxes, in terms of voter support, increase disproportionately when they rise faster than the growth of the economy as a whole.

Even though studies show that many voters are unaware of the actual tax rate this does not imply that they are unaware of the presence of tax increases (or decreases), i.e. the time derivative of the tax rate (see e.g. Wahlund, 1991). If this is the case voters would punish the government more in the first case than in the latter. This can be tested by regressing taxes against the support for the governing party/parties as measured in opinion polls or in actual elections. The fact that parties have promised higher taxes if they win the election – and won, e.g. in the national election in 1994 – indicates that tax hikes per se is not enough to scare voters away.

4. Are You Better Off Now than Four Years Ago? The Use of Misery Indices in Politics

The third field of research of relevance here is the empirical use of “discomfort” or “misery” indices. The concept was invented by economist Arthur Okun and is usually simply the sum of the inflation and the unemployment rate (Okun, Fellner & Wachter 1975). These indices have proven good predictors of elections. Using the change in the misery index from the inauguration to the next election we can for example predict the outcomes of most presidential elections in the US. The only post-war election outcomes that contradict the predictions of the misery index is the Eisenhower reelection victory in 1956, the Nixon reelection victory in 1972 and the G W Bush election victories in 2000 and 2004.¹⁰ In Sweden too, the misery index is a fairly good predictor of election results on the national level. Since the unicameral system was adopted in 1973, the change in the misery index can predict the winner of all national elections with the exception of the elections in 1979 and 1994.¹¹ It should however be noted that the number of cases are small so a great degree of caution should be applied before drawing any conclusions.

However, it is unreasonable to assume that this will be the case on the municipal level because unemployment and inflation are policy variables that the local politicians cannot affect. Instead the tax rate would be the major economic policy variable on the municipal level.

The prediction power of misery indices give a clear indication that voters care about macroeconomic factors when they evaluate political performance and that the misery index variables should be used as controls in studies that are looking into economic voting. The assumption, however, is that the misery index variables will play a limited role in explaining the outcome of municipal elections.

¹⁰ www.miseryindex.us

¹¹ See appendix B

5. Hypothesis and model

The hypothesis in this paper is that voters use economic growth of the economy as a reference point when they evaluate municipal tax policy. Municipal politicians that increase taxes at a higher pace than the economic growth are thus assumed to lose electoral support to a much larger extent than those who have raised taxes at a slower pace. That is, if the electorate is of the opinion that things are heading in the right direction, i.e. if they are better off (in relation to the reference point) they are expected to support those that are in power at the time. If they believe that things are heading off in the wrong direction, they are expected to vote for change.

This will be tested by using a model in which the effect on voter support for the governing majority is a function of the tax rate, changes in the tax rate, and general macroeconomic variables. The model that will be estimated can be written as follows:

$$Y_{it} = \alpha + \beta_1 * Tax_{it} + \beta_2 * Dtax1_{it} + \beta_3 * Dtaxelec_{it} + \beta_4 * Dummy1_{it} + \beta_5 * Dummyelec_{it} + \beta_6 * Inf_{it} + \beta_7 * Unemp_{it} + c_i + k_t + u_{it}$$

Y is here the change in support for the governing majority since the last election; Tax is the current tax rate in percent; $Dtax1$ is the change in the tax rate the last year; $Dtaxelec$ the cumulative change in the tax rate since the last election; $Dummy1$ and $Dummyelec$ are dummy variables that captures the abovementioned reference point effect; Inf is the change in the inflation rate since the last election and; $Unemp$ is the change in the unemployment rate since the last election. In the regression municipalities are used as group variables and years as time variables.

The calculation of Y is straightforward. For each municipality the voter support for the governing majority is calculated. This figure is then compared with the support for the same parties (even if they no longer is the ruling majority) in the next election. Neither is the calculation of the tax rate complicated, being the actual tax rate in the municipality. The variables for change in the tax rate in absolute terms indicate whether and how much the tax rate has changed the last year and since the last election.

The dummy variables are defined by comparing the change in the tax rate in a municipality with the change in economic growth. If the change in the tax rate is larger than the economic growth the dummy variable is set to 1, and to 0 otherwise. This implies that the dummy is 1 where taxes would be experienced as taking something from the voters (i.e. they are experiencing a loss). Under the assumption that the hypothesis is correct we will expect that the dummy variables are more important in explaining the change in voter support than the variables indicating absolute change. Previous research has shown that voters are short-sighted and we can therefore also expect that the impact of the changes in the tax rate in the last year is more important than the change since the last election.¹²

12 Nannestad and Paldam 1994 p 217, 238 shows that voters often disregard changes in the economy that have taken place more than a year ago when they evaluate government performance.

GDP growth is a here proxy for the average well being of the economy. Growth figures for municipalities are hard to calculate and are often misleading due to the fact that municipalities and local labor markets in many cases do not coincide. Even if municipal growth data were available we are examining how voters react to perceived growth and it would therefore still have been reasonable to use GDP as a measure because GDP is the measure used in the political debate.¹³

Inflation and unemployment are used as control variables. These are factors that the local politicians are unlikely to affect and voters would according to theory not take changes in inflation and unemployment into consideration when they evaluate the performance of the municipal government. The annual change in consumer price index (CPI) is used as a proxy for inflation. As the measure of unemployment, “open unemployment” i.e. unemployment among people 16–64 years old (excluding students and people taking part in labor market training programs) is used. Until 2007, this was the common measure of unemployment in Sweden and the measure that the voters are familiar with. The expectation is that these variables will have little impact on municipal voter support.

Theory gives preference for neither the random effects nor the fixed effects model, so both will be used to test the hypothesis.

5.1 Data

In order to test the model a new and extensive data base containing municipal tax rates and municipal election results has been created. The data base comprises all Swedish municipal elections from 1976 to 2002 in addition to the municipal tax rates for all municipalities during this period. In all, the data base contains 18,560 observations about election results and 5,510 observations about tax rates. For each municipality and election, the governing majority has been indicated. This differentiates this data base from earlier attempts to develop such data bases. In Petterson-Lidbom (2008) for example, the assumption has been that the coalitions – “blocks” – that compete for power always comprise the same parties. In reality the coalitions do not always look like that. Instead there are municipalities that are governed by coalitions reaching across the block boundaries (i.e. containing parties from “both sides of the aisle” as they are typically organized in the national Parliament) or coalitions that contain parties that are not represented in the national Parliament, for example parties that are specific to a particular municipality or parties that have yet to achieve a breakthrough at the national level.

By using municipal election data it is possible to isolate the effects of tax policy to a great extent. Due to the legal status of municipal politics in Sweden, the tax rate is the only major policy variable the local politicians can change independently. First, the municipalities can tax only income from physical persons (as opposed to legal persons like corporations), and only as a proportional tax – and the municipal taxes paid by the residents are not deductible from income for the purpose of calculating the tax liability at the national level. Nor are municipalities allowed to

¹³ Further elaboration on why growth figures on the municipal level are not used could be found in Larsson & Lindell 2001 or in Nygren & Person, 2001

run a budget deficit (even if this restriction is not completely binding in practice). Second, up towards 80 percent of the municipal activities are implementations of decisions made by Parliament. Only in areas concerning traffic planning, zoning and cultural and leisure activities is there a large amount of municipal self-government in practice.

There are reasons to believe that the impact of tax hikes is likely to be somewhat blurred if municipality data are used. As noted earlier the level of municipal spending is to great extent decided by national law and the inter-municipal redistribution program in effect sets a floor of taxation and spending. In this paper the effect of tax hikes, not of tax (or spending) cuts, is the area of study, so the effect might be minimal. Of greater concern is the fact that changes in national (or county) tax policy could hide changes in municipal tax policy. Voters might consider the total taxes paid rather than the composition of local and national taxes.¹⁴ It is however rare that local tax hikes are cancelled out by national tax cuts (due to the infrequency of the latter) so the effect might in reality be small.

5.2 Exploring the Data

The database consists of 2 320 observations of local election results in Swedish municipalities from 1976 to 2002. Some general observations can be noted: The variance has decreased significantly over time. In 1976 the municipal tax rate varied from 10.6 per cent to 17.97 per cent. In 2002 on the other hand the high and low marks was 17.28 per cent to 23.57 per cent (in both cases excluding municipalities such as Gotland and Gothenburg that were not part of a county [landsting] with its own power to tax). The median in 1976 was 16 per cent compared to a median tax rate of 21.3 per cent in 2002. The decrease in variance is probably a result of increasing difficulties in increasing already high taxes and decreasing marginal revenue of taxation.

From a statistical perspective the reduction in variance over time means that it is harder to get significant estimates in the regressions made. The large population will however probably compensate for this drawback. It is also to be noted that tax hikes the year before an election are as common as tax cuts. One explanation could be that politicians in power try to avoid raising taxes but if they fail to balance the budget (municipalities cannot legally run deficits) they will choose to raise taxes rather than cut spending. Benefits are often targeted but municipal taxes can only be proportional (implying a broad tax base), which means that the rulers would face stiffer and more well-organized opposition if they try to balance the budget by cutting spending instead of raising taxes.¹⁵

14 When taxes are actually paid may also play a role. If all taxes accrued during the previous four-year period would have to be paid in cash by the voter when entering the polling station, this would possibly totally change the composition of the parliament.

15 This is an explanation derived from interest group theory (Olson 1962). That different theories can be used to explain the same phenomena, or that different theories could explain different parts of a phenomenon is natural in a world of multi causation. A measure of caution should therefore be taken before saying that a specific theory is *the* explanation to a specific phenomenon.

6. Results

The model was estimated with both random (table 1, appendix A) and fixed effects (table 2, appendix A). The choice of estimation did not affect the results. The regression shows that there is a significant effect of *Dummy1* on election results. The coefficient estimate for *Dummy1* is 2.54 in the random effects model and 2.56 in the fixed effects model. This could be interpreted as meaning that the ruling coalition loses on average 2.5 percentage points of their support in an election if the tax rate in the municipality has been increased by more than the growth of the general economy during the year prior to the election. At the same time the coefficient estimates for tax hikes in general (*Dtax1*, *Dtaxelec*), tax hikes larger than the general growth since the last election, and the tax rate (*Tax*) are insignificant, which means that none of the controls appear to be involved and that the voters only react to the changes that takes place short before the election (the latter is just what Nannestad and Paldam 1994, have shown earlier). As assumed, inflation and unemployment are insignificant.

The R^2 however, are in both regressions so low that a great degree of caution must be taken. The results are consistent with theory when it comes to the sign of the coefficients and the size of the coefficient is large enough to merit consideration. The statistical significance is high but the practical significance is, as a consequence of the low fraction of explained variance, quite low. This means that the model should not be used to make predictions about how fiscal policy will affect the results of any one election. The behavior of voters on Election Day is too complex and influenced by too many factors to enable us to make predictions about election results using a model with so few variables.

7. Concluding Discussion

The idea behind this paper was that politicians have tacit knowledge, as indicated by e.g. then Prime Minister Göran Persson, of the impact of psychological factors on voters. The implications of this assumption on the specific area of municipal tax policy and loss aversion was tested using data from all municipal elections in Sweden 1976 to 2002. The hypothesis was that we would see a smaller reaction to tax increases that left the voters worse off (in the paper the real growth is used as a proxy for general economic well being) than to increases that left them with less in their pocketbooks. That is, voters would punish the ruling majority by not voting for them in the latter case but not in the former.

The hypothesis was tested using panel data regression. The results show that voters indeed do punish the ruling majority when theory predict they will and that they do not punish them fairly when theory predict they will not. It can also be concluded that voters have fairly short memory.

The adverse effect on voter support is significant when taxes increased more than the growth of the economy in the year before an election; however there is no significant effect when the growth of the cumulative tax rate was more than the cumulative growth of the economy since the last election.

The adverse impact of tax hikes on voter support might however be the result of bad economic management because inefficient management of funds might lead to demands for higher taxes in a situation where the municipalities cannot legally run deficits.¹⁶ This would have implied effects also on the tax rate, but the estimate on this coefficient is insignificant. The estimates of the misery index controls are also insignificant. Inflation and unemployment might not be the perfect proxies for good macroeconomic management but are the standard ones. One reason might be that voters care less about the economic performance on the national level than about ideology, thus limiting the spillover effects of successful or unsuccessful economic governance by the national government. An interesting idea for further research is to examine whether there is a correlation between the party/coalition in power on the national level and the voter support for the same party/coalition on the local level, when, controlling for policy as is done in this paper.

To conclude this paper shows that voters on the local level seem to behave according to the implications of the economic-psychological theory regarding loss aversion and that tax hikes are “free” in terms of voter support as long as they are not too large and don’t take place just before an election.

The paper also lends support to the rationale behind the reformist strategy of the Social Democrat party which ruled Sweden most of the time since the adoption of universal suffrage: It is possible to build a massive welfare state as long as it is done incrementally and as long as voters/tax payers are left to

¹⁶ In 2005, i.e. after the period studied in this paper, the restrictions on running deficits were relaxed somewhat (prop 2003/2004:105)

enjoy a part of the economic growth in form of increasing real wages. The results – and the theories used – can therefore serve as a remedy for more traditional theories such as Public Choice, which have serious difficulty in explaining the longevity and the popularity of the Social Democrat high tax Swedish welfare state.

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Appendix A

Random-effects	GLS regression	Number of obs =	2320
Group variable	(i): municipality	Number of groups =	290
R-sq: within	= 0.0277	Obs per group: min =	8
between	= 0.0003	avg =	8.0
overall	= 0.0243	max =	8
Random effects	$u_i \sim$ Gaussian	Wald chi2(7) =	57.54
corr(u_i , X)	= 0 (assumed)	Prob > chi2 =	0.0000
dvar std	Coef. Std. Err.	z P>z [95% Conf.	Interval]
tax	-.0001382 .0005122	-0.27 0.787 -.0011422	.0008658
Dtax1	-.0031921 .0030293	-1.05 0.292 -.0091295	.0027454
Dtaxelec	-.0000703 .0012432	-0.06 0.955 -.002507	.0023663
Dummy1	-.0252403 .0060917	-4.14 0.000 -.0371797	-.0133008
Dummyelec	-.0100395 .0081481	-1.23 0.218 -.0260096	.0059305
unemp	-.0013118 .0017845	-0.74 0.462 -.0048094	.0021859
inf	.002187 .0010179	2.15 0.032 .000192	.004182
_cons	-.0165702 .0150844	-1.10 0.272 -.046135	.0129946
sigma_u	0		
sigma_e	.07409341		
rho	0 (fraction of variance due to u_i)		
Fixed-effects	(within) regression	Number of obs =	2320
Group variable	(i): municipality	Number of groups =	290
R-sq: within	= 0.0279	Obs per group: min =	8
between	= 0.0015	avg =	8.0
overall	= 0.0238	max =	8
F (7,2023)	= 8.30	Prob > F =	0.0000
corr(u_i , Xb)	= -0.0093		
dvar std	Coef. Std. Err.	z P>z [95% Conf.	Interval]
Tax	0.0002344 .0008972	0.36 0.718 -.0014352	.002084
Dtax1	-.0050013 .0032796	-1.52 0.127 -.0011433	.0014304
Dtaxelec	-.0000931 .0013369	-0.07 0.944 -.002715	.0025288
dummy1	-.0256359 .0062442	-4.11 0.000 -.0378816	-.0133902
dummyval	-.0081562 .0083104	-0.98 0.326 -.024454	0.0081416
unemp	-.0016477 .001802	-0.91 0.361 -.0051817	.0018864
inf	.0024134 .0011267	2.14 0.032 .0002037	.0046231
_cons	-.0246406 .0212571	-1.16 0.247 -.0663287	.0170475
sigma_u	.02614253		
sigma_e	.07409341		
rho	.11070835 (fraction of variance due to u_i)		

Appendix B

Sweden

Year	Misery	Dmisery	Win/Loss	Prediction
1976	8,3			
1979	9,3	1	Win	Loss
1982	11,8	2,5	Loss	Loss
1985	10,2	-1,6	Win	Win
1988	7,5	-2,7	Win	Win
1991	12,6	5,1	Loss	Loss
1994	10,2	-2,4	Loss	Win
1988	6,4	-3,8	Win	Win
2002	6,2	-0,2	Win	Win

United States

Year	Misery	Dmisery	Win/Loss	Prediction
1948	11,49			
1952	5,32	-6,17	Loss	Win
1956	5,64	0,32	Win	Loss
1960	7	1,36	Loss	Loss
1964	6,44	-0,56	Win	Win
1968	7,83	1,39	Loss	Loss
1972	8,87	1,04	Win	Loss
1976	13,45	4,58	Loss	Loss
1980	20,76	7,31	Loss	Loss
1984	11,81	-8,95	Win	Win
1988	9,57	-2,24	Win	Win
1992	10,52	0,95	Loss	Loss
1996	8,34	-2,18	Win	Win
2000	7,35	-0,99	Loss	Win
2004	8,21	0,86	Win	Loss

Dmisery is the change in misery index since the last election. Win/Loss shows whether the incumbent president or party/coalition won or lost the election and prediction what the misery index would predict.

The Municipal Takeover of the School System

Erik Lakomaa

Abstract: In 1992 the Swedish school system was transferred from the State (the national level) to the municipalities. The reform increased the size of the municipal sector by one fifth, making the reform one of the largest in recent history. Despite broad support for the reform in Parliament, the process was very slow and discussions went on for some twenty years before the final decision was made. Traditional economic theories might be less suitable to explain both the slow process and the outcome of the reform. In this paper insights from economic psychology are used as remedy for the lack of explanatory power of traditional economic theories. The paper covers the political process that preceded the reform, an evaluation of the economic consequences of the reform and an attempt to explain some of the particularities of the reform using economic-psychological theories. The paper also provides a background to public sector reforms in general.

For discussion and valuable comments I would like to thank Richard Wahlund, Håkan Lindgren, Örjan Sjöberg, Bengt-Åke Berg, Karin Råde, Hans Sjögren, Marie Johnsson and seminar participants at Stockholm School of Economics. Thanks also to Christoffer Rydland for valuable comments and help with data. Financial support from the Jan Walander Foundation is gratefully acknowledged. All remaining errors are solely mine.

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1. Introduction

Welfare reforms are an area of research that has attracted a fair amount of interest in recent years. A subset of the reforms is about transfers of public activities from one jurisdictional level (nation, county or municipality) to another. The “municipalization” of the schools, i.e. the transfer of responsibility from the national to the municipal level, which was implemented in Sweden in the 1991/1992 academic year, is in this context one of the most far-reaching. Schools, after the reform, comprised about one fifth of the municipal obligations and more than 115 000 people did, in reality, change employers, from the national government to the municipalities.¹ Going back all the way to when the schools were made a responsibility of the national government – this process was finished in the 1972/1973 academic year² – the issue of “re-municipalizing” them has been discussed. When the decision about municipalization was finally made, just shy of twenty years later, there was widespread political consensus about the desirability of the change of responsible party. However, there were some dissent about how and when this reform should be implemented, which resulted in a wide-ranging public debate both before and after the transfer of responsibility.³

Despite the size of the reform, it has not heretofore been the object of any wide-ranging academic research. On the other hand, the reform was discussed to a significant extent in the media, both before and after the decision. In this, the reform differs dramatically from the concurrent municipalization of elder care (“*The Ädel Reform*”), which – despite a similar economic size – received relatively little media attention.⁴

The purpose of this paper is partly to describe the process that lead up to the implementation of municipalization, partly to analyze the process and its consequences, with a starting point in economic-psychological theory. Unlike traditional theories, economic-psychological theory observes that people are not strictly ratio-

1 The teachers were employees of the municipalities, but salaries and conditions of employment were earlier fixed by the national government, and the responsibility for personnel was therefore split. According to The National Agency for Education (1993), there were 86,727 teachers at the grade school level (grades 1 through 9) and 28,941 teachers at the high-school level, (corresponding to 75,357 and 22,230 full-time positions, respectively). Göran Persson (2007 p. 54) claims that the reform comprised 200,000 teachers, this is not accurate.

2 The decision was made in 1969

3 See for example the editorial in Dagens Nyheter – the largest morning paper – on August 18, 2007: “*Minister of Education Jan Björklund cannot make the the mistakes by Göran Persson undone. To transfer the schools to the national level would just be to repeat them. [...] The first priority for the Minister of Education was to municipalize. All other concerns were secondary. In itself, the idea that the schools should be municipalized was not completely wrong-headed. The responsibility for the schools had been divided earlier, and like all dual-command structures, it had created a lack of clarity. Through municipalization, school policies could be adapted to local conditions. The negative side of this development was reduced equality and sometimes a hollowed-out quality. But, on the plus side, there were the possibilities of working more efficiently and let loose creativity.*” See also the statement from the Minister of Education, Jan Björklund, in Svenska Dagbladet (another leading morning paper) of August 17, 2007 that a re-transfer to the national government would produce “*increased equality, increased status for the teaching profession, better results.*”

4 See Lakomaa 2008

nal and that they often use rules of thumb, *heuristics*, when making decisions. Both experiments and empirical studies have shown that these theories have significant explanatory power in many domains. Not leastly, this applies to decisions in financial markets and to consumer behavior. The assumption that the same decision models that have proven applicable in these contexts should be applicable also to political decision-making is not a very strong one.

The goal of this paper is not to try to confirm or falsify the economic-psychological theories, but to use them with the intent to complement and develop classic source criticism. To the standard source criticism criteria a further criterion is added. Are the statements in the source material consistent with the predictions that are supplied by the theory?

The distribution of tasks between different levels of government can be understood from a long list of theoretical starting points; the ones used most frequently in recent years are the public choice and rational choice schools of interest-based models, and also institutional theory (Arrow 1968, Elster 1986, James Buchanan 1959, James Buchanan & Tullock 1962, Mueller 2003, Olson 1962, Coase 1960, North 1990, North 2005).⁵ All of these theories can to varying extent be useful for the understanding of the events described. Here, however, there is an attempt to push the analysis further with the aid of the exploits within economic-psychological theory.

Several different economic-psychological theories might be useful here, such as the *Prospect Theory* (Kahneman & Tversky 1979, Thaler 1980, 1985, Tversky 1981, Tversky 1992, Wakker & Tversky 1993, Rabin 2000, Rabin & Thaler 2001, Wahlund 1989, 1991); *Mental accounting* (Thaler 1980, 1985, Arkes & Blumer 1985, Kahneman, Knetsch & Thaler 1991); *reference point theories* (Kahneman 1992, Bazerman & Neale 1991) and *Proximity Effects*, which mean that the decision maker is affected by the closeness to those who are affected by the decisions (Milgram 1963, Kilhan & Mann 1974, Latané 1981, Latané & Wolf 1981, Tanford & Penrod, 1984 Trope & Liberman 2000). These theories have obvious applications with regard to welfare reforms (which are all about changes), and transfer of tasks from one jurisdictional level to another (that the decisions move either away from or towards the voters or the users).

The paper first examines the source material, after that there is a description of the general political-economic development which led to that it became relevant to discuss transfer of public activities from one jurisdictional level to another in the first place. After that follows a historical description of the economic results of the reform, and finally an analysis of which mechanisms can be assumed to be behind the decision and its consequences.

5 For Swedish applications see e.g. Gennser (1982), Jordahl (2002), Sanandaj & Wallace (2003), Rothstein (1986), Rodriguez (1981).

2. Source Materials

This paper is based partly on official publications in the form of state-sponsored studies, propositions (bills originating from the Government), motions (bills originating from Parliament members or groups) and minutes from Parliament⁶, and partly on articles in newspapers and professional magazines. As a complement to the printed material, interviews have been done with a number of those who were key persons in the described process.

In several cases, the paper is based on statements from people, statements that can be found both in minutes from Parliament and in motions (bills originating from Parliament members or groups), their own memoirs and similar sources, and in the interviews that were done for this paper. In these cases, the possibility cannot be excluded that there is a dependency between the various sources.

The use of interviews makes the same demands on source criticism as the use of other source materials. It should be noted, however, that there is a risk that the interviewee to a larger extent is more distant in time than when going back to contemporary articles in media and that there may be some rationalizations after the fact supporting the decisions made. Because of the nature of this material, it is also necessary to be alert to the possibility of personal bias. However, it is possible to see that, both across time and between the different participants, there is large consensus between the different statements concerning the overarching events, which reduce these problems. Most of the interviews were made in 2007, but the decision about municipalization of the schools was made in 1989, almost 20 years earlier. Concerning the questions that are about the discussions about limits to the growth of the public sector, those discussions took place 35 years prior to the time of the interview. As time passes, the risk increases for memory lapses or that answers are based on secondary sources. The researcher must allow for this. He should also reflect on the techniques for the interview. In this case, a so called half-open interview, that is the interviewer starts by asking open questions and then the interviewer asks more specific questions and asks follow-up questions. With half-open interviews (just like with open interviews) there is thus the risk for bias, for which the researcher needs to allow.

2.1 Persons Interviewed

The choice of people to interview was based on the desire to complement printed source materials with comments from some of those who were present during the process, as decision-makers, advisers or just as listeners. Interviews have been made with Ingvar Carlsson, Lars-Eric Ericsson, Margit Gennser, Per Borg, Bengt-Åke Berg, and Carl-Johan Åberg. Carlsson was the Social Democrat Prime Minister 1986-1991, that is during the period when the major decisions were made. He was

⁶ Motions (bills submitted by Parliament members or groups), propositions (bills submitted by the government) and committee memorandums are taken from Rixlex and therefore have no page numbers.

also Minister of Education 1969-1973 which does not only coincide with the time when the transfer of the schools to the national level was finalized, but also with the time when re-municipalization first started to be discussed and studied. Lars-Eric Ericsson is a Social Democrat, and was the chairman of the Association

of Swedish Municipalities 1986-1992. Before that he was a city council member in the Municipality of Uppsala (1974-76) and he was under-secretary of state in the Ministry of Culture (1974-1976), Margit Gennser was a member of Parliament for the Moderate Party (Conservative) between 1982 and 2002 and was, during the eighties, her party's person responsible for municipal issues. She has a background as a municipal politician in Malmö. Carl-Johan Åberg is a Social Democrat and was under-secretary of state in the Ministry of Finance under Gunnar Sträng and responsible, in 1971, for *Långtidsutredningen* ("The Long-Term Study", an ongoing planning tool in Sweden). As under-secretary, he was a central actor when issues about efficiency and the determination of primary responsibility first were brought into discussion.

Bengt-Åke Berg is a Social Democrat and was Budget Chief in the Ministry of Finance during the first half of the seventies, under Gunnar Sträng, and as such he had considerable knowledge of the policies of budgeting. Later, he became the supervisor for social issues in the City of Stockholm, and in this role he came to see the process from the municipal point of view. Per Borg, also a social democrat, was under-secretary of state – although in a ministry not affected, the Ministry of Defense – during the period when the decisions about the great changes in primary responsibility in the public sector were made. He has also written his Doctoral Dissertation on political reform processes. (Borg 2004).

The main actor in this description was without a doubt the then Minister of Education, Göran Persson. Unfortunately, it has not been possible to interview him, but he writes about the issue in his memoirs (Persson, 2007). However, it is somewhat surprising how little he comments. The whole time he was Minister of Education is described on five pages, and the transfer reform on less than one page. For the rest, it can be said that the central actors are the then Prime Minister Ingvar Carlsson; the Chairman of *TCO* (Swedish Confederation of Professional Employees), Björn Rosengren and the then under-secretary in the Ministry of Education, Anitra Steen⁷. Of these, Carlsson was willing to give an interview.

The source material largely shows, however, a consensus, so the fact that Persson could not be interviewed is less serious than it could have been. However, there is a risk for collective forgetfulness or bias, which can be caused by rationalizations after the fact or that the interviewees base their answers on sources they have in common. One problem in this context is, however, that it is precisely Persson's own description that deviates the most.

Several of the interviewees have also written memoirs, which have been used as source material. Few of these, however, discuss the municipalization of schools, that applies to those of Carlsson (2003) and Åberg (2006). Three of the interviewees (Gennser 1982, Åberg 1997, Borg 2006) have, in other contexts, written about

⁷ Persson later married Steen

how it is possible and how to go about reforming the public sector. They do not, however, use the schools as an example.

During the work with this paper, all memoirs and similar that were written by Government ministers during the period in question, have been gone through. Among these, there are descriptions of the period in question from actors who are or were Government ministers, for example Feldt (1991), Leijon (1991), Andersson (1993), Sahlin (1996), Hellström (1999) and Peterson (1999), but they do not mention the school reform either. Perhaps this tells us something about what little importance this issue was regarded as having, and, at the Government level, at least, how uncontroversial the question was regarded, among many in politics. Persson, however, does write about “*a violent political struggle*”⁸ but it is not clear whether he means that there was a struggle within or outside of Parliament. If he means the latter, his description is compatible with those given by the other sources, otherwise not. It is possible to think that Persson wants to portray the resistance to the reform as bigger than it was, to make his own efforts more important. Whether this is the case cannot be determined. At the same time that he exaggerates regarding how many people are included in the reform⁹ he rather understates its importance:

The so-called municipalization reform which Anitra [Steen] and I pushed through did not really consist of anything except that the entirety of the employer responsibility for all teachers who served in the municipal sector was transferred to the municipalities.¹⁰

However, none of the other sources try to downplay Persson’s role, rather the opposite, but, unlike Persson, they often highlight how wide-ranging this reform was.

8 Persson 2007 p 54

9 Persson was of the opinion (2007 p 54) that there were 200,000 teachers that were included in the reform, at a time when all teachers at grade and high-school levels comprised only 115,000.

10 Persson 2007 p 54

3. Turning Points in the Welfare State

The Swedish example shows that it was possible to combine a substantial growth in public commitments with substantial economic growth. During the period 1950 to 1970 GNP increased by on average 4 per cent per year, at the same time that public expenditure increased from 24.7 to 43.9 percent of GNP. Public consumption increased at the same time from 12.6 percent to 21.8 percent. (Here, “public consumption” excludes transfer payments). This means that the public sector grew almost twice as fast as the economy as a whole. In 1980, public expenditure was 62 percent of GNP and public consumption 29.3 percent.¹¹

However, during the 1970s, it became increasingly clear that the path on which the nation was embarked was not sustainable in the long run.¹² Sweden was no longer a low-tax country, but instead one of the countries in the world with the highest taxes. During the period when Gunnar Sträng was Minister of Finance (1956-1976) the tax burden increased from 27 to 48 percent.¹³ However, even he started to realize that this development could not go on forever.

[Sträng] was completely aware that the Swedish economy as early as in the late 1960s had started to weaken. Inflation increased, competitiveness weakened, and the deficits in foreign trade increased. He was not alone in the Department of Finance to observe this picture. A large number of his subordinates shared his opinions. He was also quite convinced that these developments constituted a threat against our earlier so strong economy and could not be fought by spreading purchasing power indiscriminately, but only by imposing a tight and restrictive policy aimed primarily at strengthening the position of the exporting industries. Here also, he had strong support from the majority of his subordinates.¹⁴

That the Swedish model would have to be re-examined became clear even during its heyday. In 1967, a Department of Industry was established, headed by Krister Wickman, to handle the reworking of Swedish industry. Even if many in the Department did not share the view that a governmental industrial policy was the solution to the problem, Åberg and Berg are of the opinion that there nevertheless was an understanding about the problems of declining productivity and with the balance of trade.¹⁵ That the expansion of the public sector could not continue unabated as earlier was also clear and was expressed in the 1970 *Långtidsutredningen* (“The Long-Term Study”, an ongoing planning tool in Sweden).¹⁶

The general principle when the modern welfare state began was, as exemplified with the workman’s injury insurance payments which was introduced in 1901, that the national government determined how much the employers should pay. The money did not – just as it did not with the national pension funds – get included in

11 Björklund & Larsson 2005 p 3

12 SOU 1971:70 p 22, Borg (2004) describes how, as early as in 1978, the realization had set in that the ATP (government pension) system was not sustainable in the long term. However, it took another 15 years from this insight until the system was reformed.

13 Edvinsson 2005

14 Åberg 2006 p 152

15 Åberg interview 2007, Berg interview 2007

16 SOU 1971:70 p 22f, 32f

the national budget.¹⁷ In step with the increased scope of the welfare policies, ever larger parts ended up under the domain of the national government, but when it was not politically or economically possible to further increase the national budget, expenses were transferred to employers, municipalities or individuals.

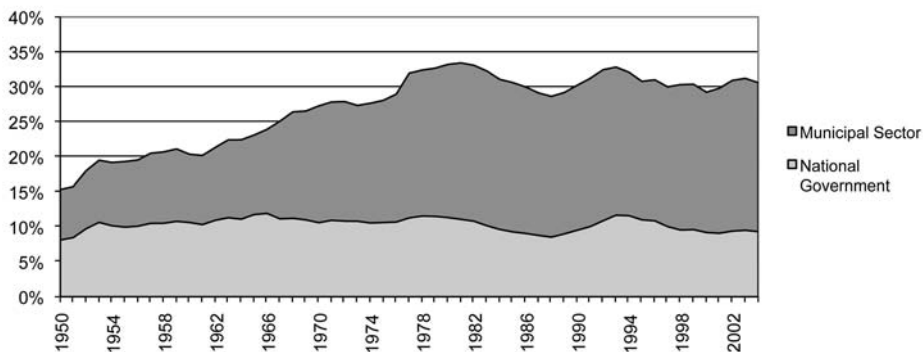


Diagram 1a: Public consumption and investments for municipalities and counties and nation as a proportion of GNP 1950-2002. Source: Björklund & Larsson 2005 p 3

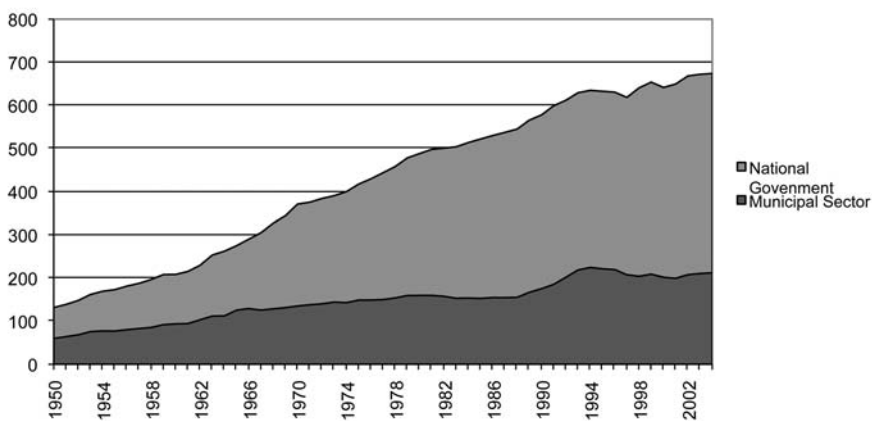


Diagram 1b: Public consumption and investments for municipalities and counties and nation in Billion SEK (2004 prices)1950-2002. Source: Björklund & Larsson 2005 p 3

¹⁷ Borg 2006 p 61

From the end of the expansion period, i.e. from the middle of the 1970s, the municipalities did take over a large part of the increase of public expenditure, simply through keeping up the expansion in spite of the fact that there was belt-tightening at the national level. The municipalities expected an increase of about four percent per year, which meant that expenses as percentage of GNP would increase as long as economic growth was less than that.¹⁸ The period studied distinguishes itself also by the fact that both indirect taxation (i.e. sales taxes etc.) and public savings (through the ATP [pension] reform) increased very strongly. That made it possible to have a serious increase of public expenses without the need to raise income taxes to the same extent. The funds that had been built up within the ATP-system also came to function as a buffer that enabled an increase of public consumption even after the growth of the tax-supported national government consumption had started to diminish. Åberg is of the opinion that Sträng was also well aware that the ATP-system had this effect.¹⁹

The large increase in public expenditure took place in the municipalities. The municipal taxes, and the corresponding expenditures, increased from an average of 14.9 percent in 1976 to 21.2 percent in 2002, and it was the municipalities with the lowest taxes that increased them most on a percentage basis.²⁰

Even before this time, large increases in the municipal tax level took place. When, in the tax reform of 1970, taxes were lowered for employees in the lower strata and at the same time the progressivity was increased, the tax reduction that would have come to the less well paid was partly eaten up by the corresponding increases in municipal taxes. The result of the reform instead became, instead of a tax reduction for people with low incomes, a large increase of the total tax burden, where the fraction of taxes levied by the municipalities increased.²¹

However, the costs for public activities increased not only by that the public sector committed itself to new tasks. There were also processes within the system that drove up costs. Wages in the public sector generally increased as rapidly as within the private manufacturing industry, where the increase in productivity has been large, this in spite of the fact that it has not been possible to measure any significant productivity increase in the public sector. Productivity in the public

18 Berg, interview 2007. Carlsson, interview 2007, is of the opinion that there probably was such an expectation but that it was not necessarily tied to the exact number four percent. In *Långtidsutredningen* 1971 (see above) a questionnaire from the municipalities is shown, which depicts an expected growth of municipal consumption of about 6 percent per year, whereas the national government expects an increase of 3.5 percent per year at the national level. In *Långtidsutredningen*, a growth in public consumption of about 4,5 percent per year during the 1970-1975 period is expected. SOU 1971:70 p 32-33

19 Åberg, interview (2007), see also Molin 1965 about the process concerning the ATP-system

20 Lakomaa (2007). The municipality with the lowest income tax in 1976 had 11.1 percent and the one with the highest had 17.25 percent. In 2002, the corresponding tax rates were 17.2 percent and 23.57 percent, percent, in both cases, municipalities that were not part of a county, that is Gothenburg, Malmö and Gotland, are excepted. It should be noted here that the actual municipal tax rates are lower than those that were expected in *Långtidsutredningen* of 1971, which expected that if the municipal expansion were to continue at the rate it had up to that point, the municipalities and counties together would have to levy 25 percent in taxes as early as in 1975. SOU 1971:70 p 33.

21 Berg, interview 2007

sector has even been negative during large parts of the period studied. The productivity increase in the public sector during the 1970s was -1.5 percent per year, and was -0.4 percent per year during the 1980s.²² This process was strengthened by the “solidaric wages policy” formulated by Rudolf Meidner during the 1950s. The “solidaric wages policy” had as a goal to contribute to the structural redevelopment in industry by setting wages based on the most productive industries, that is the export industries. The policy would have as a consequence that less productive activities would be forced out, and the employees could then be put to more productive tasks. This, however, was only applied to activities exposed to competition.

For the public sector, the “solidaric wages policy” instead meant that the costs increased. Municipalities and national offices were of course not shut down if the productivity of the employees was less than their salary costs. The “solidaric wages policy” also had as a result that the public sector absorbed some of the people who were left without employment when low-productivity companies went out of business. To some extent, this wage expansion in the public sector has been counteracted by the fact that the employees have not had any alternate employers to turn to if they were dissatisfied with their wages. For a long time, this was true of teachers, including pre-school teachers, and personnel in the “caring” professions. The “solidaric wages policy” has thus not been carried out fully within the non-competitive public service sector, even if it has of course been affected by the fact that this wage model has been applied in other sectors.

Salary costs (including payroll taxes) are, together with demographic changes, the main causes of the fact that the Association of Swedish Municipalities has expected that even in this day and age seriously increased municipal taxes will be needed to finance the same activities as today into the future.²³ This phenomenon was something that worried Strång and his subordinates in the Ministry of Finance all the way back to the mid-sixties. Because the productivity in the public sector did not increase at the same rate as the wages, the costs would increase to such an extent that in the long run they would crowd out other public programs that were not tied to wages, such as investments in infrastructure. However, no solution to this problem was discussed at the Ministry of Finance.²⁴

22 Lundgren (2007). Looking at the whole period from 1971 to 2001, productivity increased by 0.2 percent per year, which means that the improvement in productivity was considerable after 1990. During the same period, productivity in the economy as a whole increased by 1.9 percent per year. Schön (2007, p 483). Within manufacturing industry, the productivity increase 1975-1980 was 2.3 percent per year, and 5.9 percent per year after 1990 Schön (2007) p 509. Here also, we thus see a strong productivity increase during the 1990s.

23 Borg 2006 p 65

24 Åberg interview 2007, Carlsson interview 2007, SOU 1971:70 p 32

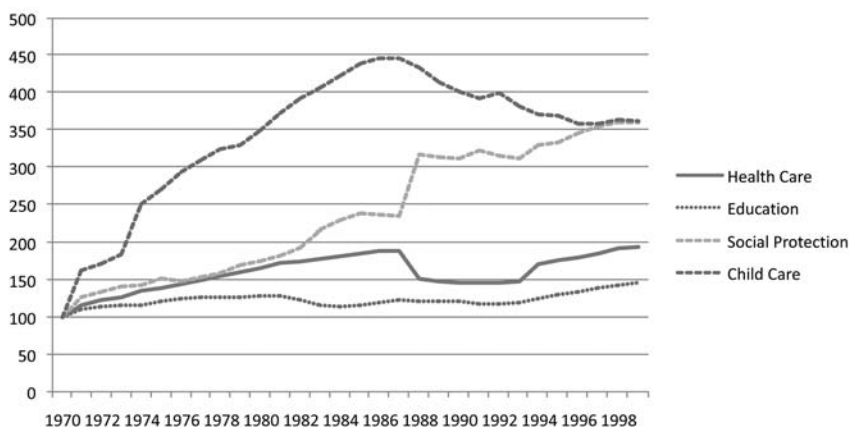


Diagram 2. Municipal expenditure for social protection (welfare payments), municipal education,²⁵ health care and child care, adjusted for the transfer of responsible party. Also adjusted to year 2000 prices. Index 1970 = 100. Source: Statistiska Centralbyrån: Tidsserier för offentlig sektor

However, it can be observed (see Diagram 2) that the development of expenditure that were municipal responsibilities (child care and social protection) increased significantly faster than activities that were handled at the national level (schools). Elder care, in spite of it being an activity for which both municipalities and counties were responsible, showed a development of expenditure that looked more like the one for schools than the one for the purely municipal activities.²⁶

That the municipalities have been the source for of large growth of government expenditure may seem both natural and unnatural. The shorter distance between the municipal politicians and the electorate can be assumed to make them more responsive to the demands for public services from the voters compared to politicians at the national level, but at the same time it could make them more sensitive to criticisms about wastefulness and suboptimal allocations.

This development should be seen in the light of the special conditions for Swedish municipalities, concerning choice of activities and the financing of municipal activities. When it comes to choice of activities, municipal self-government is severely limited. Upwards of 80 percent of the municipal activities are implementations of decisions made by Parliament. Only about issues concerning traffic planning, zoning and cultural and leisure activities is there a large amount of

25 As the high-school level had been expanded by turning the last remaining two-year study programs into three-year programs starting with the 1993-1994 academic year, it is reasonable to assume that the costs for these activities would have increased even if no other changes had taken place; these effects make it harder to observe which changes in expenditure have which causes.

26 A Public Choice approach would have given the opposite prediction. As there are more voters that are affected by elder care and by the schools than by child care and social protection (with elder care, those that use it have not only the right to vote but also a high level of voter participation) it could have been expected that primarily elder care and secondarily the schools would have expanded (there are more voters with children of school age than with children below school age, the latter being the main users of child care).

municipal self-government in practice. The municipalities can tax only income from physical persons (as opposed to legal persons like corporations), and only as a proportional tax – and the municipal taxes paid by the residents are not deductible from income for the purpose of calculating the tax liability at the national level. Nor are municipalities allowed to run a budget deficit, even if this restriction is not completely binding in practice. These restrictions on the income side brings with it the expectation that municipalities are more responsive to the wishes of the electorate than is the national government, and that interest groups should have less influence on the policies implemented.

At the same time, the municipality is in many cases the largest employer in the area, and this means that to many residents in the municipality, higher municipal expenses not only imply higher taxes, but maybe also higher wages (for a given level of service). This makes it difficult to say in advance how the residents would respond to higher municipal taxes. Earlier research (Lakomaa 2006) has shown that tax increases in municipalities do not lead to reduced voter support for the ruling majority as long as the increase is less than the economic growth, that is as long as the voters do not end up with less money in their wallets than in the previous period.

4. The Road to Municipalization of the Schools

The development of the Swedish welfare state can be crudely divided into a *formative phase*, which lasted until 1950, an *expansion phase*, which lasted until 1975 and a *consolidation phase* which followed. During the *formative phase*, it was often the local community, first the parishes (there was no separation of church and state) and then the municipalities that delivered the services. This was true regarding for example the schools, care of the sick and elderly, and the police force.²⁷ The distinguishing characteristic of this period was a steady, but not too rapid, growth of the public commitments. The *expansion phase* that followed had its own clear characteristics: large increases in the public commitments and centralization. During this period, the national government took over the responsibility for many activities that had previously been handled at a lower level. That applies, for example, to the police, the courts and the schools.

The municipal reforms that were implemented during this period also included that the number of municipalities was greatly reduced, at the same time that their size increased. After 1975, the expansion of the public sector diminished or ceased, and the changes that were made after this time were to a significant extent issues of responsibility and efficiency, that is who should finance and perform the tasks and how to get maximum use out of the tax monies. There was an extensive debate about whether public or private actors should handle different welfare services, and whether those who used the services should have any influence over them. During this phase, some activities were returned from national or county level to the level of the municipalities. This was the case for care for the elderly and disabled, among others.

The same long-term trend – first centralization and then decentralization – which was the hallmark of the public sector as a whole – can be seen with the schools.²⁸ When public schooling was first introduced in Sweden during the middle of the eighteenth century, it became a concern for the parishes, while the higher levels of education (including “*gymnasium*” or, roughly, high-school level) came to be handled at the national level.²⁹ As early as in 1949, some municipalities introduced the nine-year “Unified School” as a replacement for the earlier “*folkskola*” (grades 1-6 or 1-8) and “*realskola*” (grades 5-9 or 7-9, and admission by application), and the year after that Parliament decided that over time Sweden would implement the “unified” school system in the whole country. The Unified School, which changed name in 1962 to “*Grundskolan*” (9-year Comprehensive School), was then introduced gradually in the whole country and the process was complete with the academic year 1972/1973. The transfer of the schools to the national level was met with protests from many municipalities, and also from the teachers and their organizations which were of the opinion that the National Swedish Board of Education and other bureaucracies would become too influential.

27 It should be mentioned in this context that activities such as debt collection, tax collection and some of judicial functions were municipal responsibilities during this period.

28 See also Bergström (1993)

29 The School Commission Study in 1946 (SOU 1948:27): proposed that the municipalities should be responsible for the schools when the *unified school* was introduced. Only the latter part of the proposal was implemented, however.

At the Ministry of Finance, there was also some criticism.³⁰ That the schools were transferred to the national government was here perceived as a step away from the division of tasks that the Government had decided upon. Within the Social Democrat movement there was the opinion that the nation should be responsible for economic security and the municipalities for the production of welfare services. According to this model, the schools ought to be a municipal responsibility.³¹ The introduction of the “Unified School” was implemented in parallel and symbiotically with the merger of municipalities that was performed at the same time. A driving argument, if not the only one, for merging many smaller municipalities to a few larger ones was that a larger number of students were required to be able to fill up the many different paths of study that the Unified School was initially intended to offer.

This was the prime reason for starting the discussions about a municipal reform, as all our small municipalities – in all over 1 000 – would not be able to implement the school reform.³²

The merger of municipalities can thus be seen as a result of the school reform, rather than the other way round. Once the merger of the municipalities was implemented however, the idea of offering different paths of study – symptomatically – been largely abandoned. Even the reform of the *Gymnasium* (high-school) which was implemented during the same time period contributed to the drive for larger municipalities. The same was also true for the reforms that were made to create a more unified administration, for example the Court Reform where the jurisdiction of the cities and towns was abolished, the changes within tax administration and the transfer of the police to the national level. One reason for the mergers not being implemented faster was that the process did not have support from all municipalities. In 1969 the Parliament abandoned the earlier voluntary path; and the transfer to the national government of the schools was fully implemented in the academic year 1972/1973.

30 Åberg, interview 2007

31 Åberg, interview 2007, Carlsson, interview (2007) is of the opinion that there was an idea about who should be responsible for different tasks described above, but that this idea was not a doctrine carved in stone.

32 Persson & Sundelin 1990, p 58. Gennser, interview 2007, holds this same opinion.

5. The Background for the Municipalization

Almost immediately after that the 9-year Comprehensive School had been implemented in the whole country, the question concerning who should be the responsible party came up for discussion. The Minister of Education at the time, Ingvar Carlsson, was of the opinion that a decentralization was the next logical reform step. Before the creation of instruments for centralized control, there was a risk that the school would not be uniform throughout the country, but when these were in place, the municipalities should take over. There was also an interest expressed from the municipalities to take over the responsibility. Even the unions representing the teachers were initially favorable, because they disliked the extensive regulation of the activities by *Skolöverstyrelsen* (the National Swedish Board of Education). Their views did however change after the unions arrived at the conclusion that the municipalities could end up having easily as much influence as *Skolöverstyrelsen*.³³

The national government study, "*Skolans regionala ledning*"³⁴ (The Regional Guidance of Schools) was the first step towards the municipalization that would take place just shy of 20 years later. In the study, it was proposed that all employees would be hired by the local school boards, but that the terms of employment should be regulated by the national government. The economic conditions would be regulated by the government from this point on. The financial aspects of a municipalization, however, were not discussed at all in this study. Those were to have no role in the process, Ingvar Carlsson argued.³⁵

Two years later, the so-called *SSK* (*Skola, Stat, Kommun*, "School, State [Nation], Municipality)-study produced a memorandum which discussed whether the municipalities were capable of assuming the main responsibility for the schools. This study, however, never made a deep political impression, but it resulted – in 1978, during the time the center-right Government coalition was in power – in its final memorandum, "*Skolan en ändrad ansvarsfördelning*, SOU 1978:65" ("Schools – a Change in the Distribution of Responsibilities") which discussed municipal responsibility for the schools. It was emphasized in this memorandum that a possible "all-municipal responsibility" would have to be implemented gradually over a long time. The studies continued during the first years of the 1980s with a study from *Skoladministrativa kommittén*, (*SAK*) (the School-Administrative Committee) named: "*Förenklad skoladministration*, SOU 1980:5," (Simplified School Administration) where a decentralization of the hiring of school principals and teachers was proposed. The proposal resulted in a proposition (bill submitted to Parliament by the Government) that regulated the issue of hiring, where certain decentralizations were proposed, but the issue of who would be the responsible party was not discussed.³⁶

33 Carlsson, interview, 2007

34 SOU 1978:65 The study was also called "*Länsskolnämndsutredningen*"

35 Carlsson, interview 2007

36 Haldén (1997)

During the five years that followed after the SAK (see above) study was presented, there was almost complete silence on this issue, but in the budget proposition 1985 (1984/85:100) the issue of who should be the responsible party was again brought up. In the proposition, it was proposed that central government regulation of the appointment of school principals should be abolished. That proposition, unlike the studies from the 1970s, can be seen after the fact as the starting shot for the municipalization reform, in that the first concrete step was taken at that time in transferring responsibility for the schools from the nation to the municipalities.³⁷ In 1988 new government study³⁸ was published. This study became the base for a new proposition from the Government (1988/89:4) where it was proposed that the municipalities should take over the main responsibility for the schools. In the proposition, the municipalization is described as a way to create “*education according to the academic plan*”³⁹ but also as a way to increase the guidance towards goals, straighten out the distribution of responsibilities, give more influence to the students and their parents, and finally to create more efficient and flexible school administration and personnel policy. However, Parliament at this time did not make any decision about municipalization. The next year, the proposition was followed by a new proposition (1989/90:41) where the same ideas came back.⁴⁰ In this proposition, the Government claimed that the development that had already happened reasonably should lead to a transfer of responsibilities to the municipalities for the schools, and that the municipalities ought to take over the responsibility starting the academic year 1991/1992. This would then give school personnel increased influence over their work situation and facilitate the movement from rule based to goal based education. The proposition, after extensive debate, was passed as law by Parliament on October 26, 1989.

37 Ljunggren (1994) p 91 is of the opinion that the change process started by the Civil Department (handling government wages but also counties and municipalities) under Bo Holmberg proposed “*changes of the public sector to make it more user-friendly and less bureaucratic. People should be able to feel that it was easier to get in touch with the national and municipal governments.*” Berg. (Interview 2007) is of the opinion that there was nobody that listened to Holmberg. None of the other interviewees have touched on Holmberg when they were asked about factors that sparked the transfers of responsibility. On the other hand, both Twaddle (1999) and Pierre (1993) claim that one of the goals of the reforms was to save face for the Social Democrats. “*They were aimed at enhancing the overall legitimacy of the public administration and also at dispatching conflicts triggered by fiscal problems to the local political level.*” (Pierre, 1993 p 387) Because the public sector was perceived as bureaucratic and inefficient, reforms were necessary for the Social Democrats to be able to keep their strong electoral support. This picture, however, is not compatible with the rest of the source material, which describes the municipalization as a very drawn-out process where there was a consensus about the goals. Nor is this picture compatible with that the opposition came primarily from the unions, and from the Liberal Party.

38 SOU 1988:20 “*En förändrad ansvarsfördelning och styrning på skolområdet*”

39 That a municipalization would result in education more consistent with the national curriculum can be seen as a paradox, as it can be viewed as easier to achieve this in a centralized operation.

40 In this proposition, some additional suggestions from the government study SOU 1989:113 was included

6. The Political Debate

In Parliament at this time, there was a wide-spread consensus that the school system would have to be reformed. At the same time, there were wide-spread criticisms regarding how the reform was handled, and that it came to be confused with the concurrent union contract negotiations:

We had to, but it was done the wrong way. [The earlier] system was not manageable, for example regarding union negotiations. The teachers had two employers with which to negotiate, and were not able to bring their pay grade if they changed municipality. Also, the municipalities did not take any responsibility.⁴¹

says Margit Gennser who was a member of Parliament for the Moderate Party and responsible for municipal issues. The then Minister of Education, Göran Persson, gives a similar picture:

The teachers were already employed by the municipalities. But, it was the national government that regulated the teachers' salaries and conditions of employment, which, as a practical matter meant that the teachers had two employers. My view was, and still is, that such a split personnel responsibility carries the risk that both organizations end up being passive.⁴²

Economic factors were also brought out as arguments for a transfer to the municipalities. Mainly, the system for financing the school system was regarded as hard to comprehend, and as complicated.

The system for distribution of economic resources was completely bizarre. It was impossible to decide if the schools should have 0.941 percent or 0.916 percent of some sum of money. There were probably only a few persons in Sweden who knew in detail how the system [funding for schools] actually worked.⁴³

Even the then Prime Minister, Ingvar Carlsson, agrees that the system used at the time was hard to comprehend, and that a system with national funding as a method to direct the schools could not comprise a system with the flexibility that schools with different local conditions required.⁴⁴ The economic perspective was brought up in the proposition too and it was pointed out that the reform would bring with it that the municipalities would be able to utilize their resources more effectively. Here, there was thus an indication that a more efficient use of resources was expected as a result of the municipalization. That economic considerations would have been behind the proposal is however denied by Ingvar Carlsson.⁴⁵ Probably, the truth is somewhere in between, i.e., economy was one of several reasons that the reform was implemented.

Several of the central actors are, however, of the opinion that the main motive for Minister of Education Göran Persson was neither economic nor organizational, but was stemming from the unease he had felt from having *SÖ* (the National Swed-

41 Gennser, interview 2007

42 Persson 2007 p 54

43 Gennser, interview 2007

44 Carlsson interview 2007

45 Carlsson interview 2007

ish Board of Education) as a de facto supervisor when he was a member of a city Council.⁴⁶ The then Prime Minister Ingvar Carlsson states that there is probably some truth to these allegations, and that the municipalization most likely would not have taken place if there had not been a Minister of Education with the courage to take on the mighty teachers' unions. To get a decision about municipalization, it was necessary that the teacher's unions not show a united front against the proposal. That Persson managed to convince the Swedish Confederation of Professional Employees (*TCO*) of the advantages with municipalization was thus the key to success, according to Ingvar Carlsson.⁴⁷ *TCO* Chairman Björn Rosengren was therefore to play an important role for the municipalization. Even if the teachers' union that was a *TCO* affiliate was critical of the reform, Rosengren was a strong supporter of it. Rosengren was of the opinion that municipalization would result in a better work environment for the teachers, as the employer responsibility would become clearer. "*Two employers is often the same as no employer.*"⁴⁸ As an argument for the reform, Rosengren also raised the point that there was a general decentralization trend within the public sector and that it therefore was quite natural to municipalize the schools.⁴⁹ A decentralization would also lead to increased influence because "*interest [will be focused] on the day-to-day work that is performed by teachers and pupils and the political decisions are moved closer.*"⁵⁰ At the same time, Rosengren claimed that the warnings that the municipalization would lead to reduced uniformity were without foundation.⁵¹

In its proposition, the Government also stated that decisions would be made closer to those who were affected by them, and that communication between different groups within the schools – students, teachers, parents and other school personnel – would thus be improved. That the teachers had expressed concerns about the proposal, which among other things would result in changes to the method for appointing people to positions, was noted in the proposition. In it, the Government expressed the opinion that these issues, instead of being spelled out in laws and decrees, should be handled by negotiation between employee unions and employers or their organizations.⁵² To continue with municipal appointments but national regulation would create "*uncertainty and lack of clarity*", said the then Minister of Education, Göran Persson.⁵³ This view was shared by both the *LO* ("*Landsorganisationen*", The Swedish Trade Union Confederation, an umbrella organization for Swedish blue-collar labor unions) chairman Stig Malm and the *TCO* chairman Björn Rosengren, who, in an article published in *Dagens Nyheter* (Sweden's largest morning daily), added that municipalization was a solution that would benefit the teachers, and that uniformity would be guaranteed by setting the curriculum at the national level.⁵⁴ In his memoirs, Göran Persson gave a somewhat different pic-

46 Borg interview 2007, Gennser interview 2007

47 Carlsson interview, 2007. Carlsson also states that the teachers' unions around 1970 had been favorable to a municipalization of the schools, which had at the time quite recently been transferred to the national government.

48 Malm and Rosengren 1989

49 Malm and Rosengren 1989

50 Malm and Rosengren 1989

51 Malm and Rosengren 1989

52 Proposition 1989/90:41

53 Persson 1989

54 Malm and Rosengren 1989

ture, and he writes there both that there “*must be some room for individual judgment [...] Local deviations and adjustments must be allowed*”, and that he understood that the teachers would consider themselves losers from the reform. “[I] realized why the teachers mounted such a resistance. The connection with the national government gave them higher status compared with other municipal employees” Persson writes.⁵⁵

The main criticism from the teachers and their organizations was that through this proposal, they would lose those privileges, primarily better conditions of employment, which they had as employees of the national government, if they became employees of the municipalities. The teachers also expressed concerns that municipalization would bring with it reduced resources for the schools. This line of reasoning was addressed in the proposition by a proposal of an extra 300 million kronor (about USD 45 million) as extra provision from the government in connection with the municipalization.⁵⁶ Minister of Education Göran Persson at the same time claimed that the schools were in a crisis and that for this reason, it was necessary that the municipalities took over the responsibility for running the schools, to be able to solve the problems.⁵⁷ Most likely, he is here referring to the schools having an organizational crisis rather than an economic crisis, and that a new responsible entity would have an easier time implementing necessary changes. Ingvar Carlsson had it that there were no economic motives behind the municipalization and if it was organization, not finances, that Persson was referring to, then their two statements are consistent with each other. Additional support for this interpretation is given by Gennser, who was of the opinion that there was a wide-spread perception both among the municipal politicians and among the municipal staff that a municipalization would contribute to the solution to many knotty organizational problems. In particular, this was true of the problems which many experienced as having with an all too influential teachers’ union.⁵⁸

In Parliament, a number of motions (bills submitted by Parliament members or groups) were introduced because of the proposition from the Government. Olof Johansson, together with several other members of Parliament from the Center Party, wrote that the proposition should be voted down.⁵⁹ This because Parliament, due to how the issue had been handled, had come to be unintentionally a party to union negotiations as Parliament would decide about the teachers’ salaries and conditions of employment.⁶⁰

When the new proposition (1989/90:41) was presented, Johansson again requested that it be voted down. He obtained agreement from the Moderate (Conservative) Party members Gennser (1989/90:Ub7), Nyhage (1989/90:Ub4) and Haglund and others (1989/90:Ub5), all of whom expressed the opinion that the

55 Persson 2007 p 54

56 Prop 1989/90:41

57 Engman 1989

58 Gennser interview 2007

59 Motion 1989/90:Ub2

60 The confusion of the political process concerning the responsible party and the salary negotiations was probably the underlying cause for the conflict as depicted in the media. As it was seen as necessary (Carlsson, 2007) to have at least one of the teachers’ unions support the municipalization, there was ample opportunity to use resistance to the municipalization as a pawn in the salary negotiations. This paid off, as we will see.

proposition should be voted down because of how the issue had been handled. Gennser and Haglund argued that that the proposition should be voted down because the Swedish Agency for Government Employers (*Statens Arbetsgivarverk* or *SAV*) was of the opinion that the proposition should not be carried because they had made an offer in the union negotiations, in which no consideration of municipalization had been given, and referring to the how the government and *SAV* had handled the issues. The Moderate, Nyhage, on the other hand, requested that the proposition be turned down with reference to that the issue of how the national goals were to be achieved had not been sufficiently studied.⁶¹

The Green Party (*Miljöpartiet*), through Claes Roxberg and others, requested that the proposition be voted down referring to unresolved questions regarding government financial contributions and goal direction.⁶² They were of the opinion that those questions should be handled in Parliament concurrently with the municipalization issue. The Communists (*Vänsterpartiet Kommunisterna* or *VPK*) was more favorable than the other opposition parties, which was to be expected as the party votes in Parliament were necessary to keep the Social Democrat Government in power, and they wanted to pass the bill, on the condition that some remaining demands were fulfilled; the teachers were to have national competency requirements, the government contributions to the municipalities intended for school activities were not to be reduced, and the money should be earmarked. Additionally, the government should offer the municipalities loans to finance improvements of the physical school environment, for example resolving problems with work environment. The party also demanded that national goals for the school be set up, to prevent differences to develop between different municipalities.⁶³

Lars Leijonborg of the Liberal Party, in his motion (1989/90:Ub9), referred to that the issue of municipalization should have been addressed in Parliament before it became an issue in union negotiations, and that it would be wrong to decide this issue before achieving clarity about how the government contributions and methods of direction should be constructed. Leijonborg also highlighted the resistance to the municipalization as an important reason to turn down the proposition. Here, Leijonborg deviated from many others in the opposition by not concentrating on procedural arguments when he requested that the proposition be turned down.

Most opponents raised procedural arguments against the bill rather than criticizing its contents. For example, Gennser claimed, in spite of her proposing rejection of the proposition, that there was a wide-spread consensus across party lines that something had to be done, and that all the way back to when studies of the issue began, the obvious solution to the problems had been to dissolve the dual responsibility.⁶⁴ When Ingvar Carlsson twenty years after the decision was interviewed about how the process had worked, he fully concurred with Gennser and refers to that he as early as in the beginning 1970s had suggested that the schools should be transferred to the municipalities.⁶⁵

61 Riksdagen (1990/91) Protokoll 1990/91:44

62 Motion 1989/90:Ub3

63 Motion 1989/90:Ub8

64 Gennser, interview 2007

65 Carlsson interview 2007

Göran Persson concurs with Gennser's description that something absolutely had to be done. He writes "[T]he old system was doomed to die."⁶⁶ Gennser even claims that many people saw municipalization as a decision which in one fell swoop would solve all the problems of the school system.⁶⁷ The Political Scientist Pierre (1993) sees a clear motive for a political consensus for this type of issues. According to him, there is an interest in maintaining the legitimacy of the public administration, that transcends party-political boundaries.⁶⁸ That is, absence of a consensus will negatively affect all political parties. Here, what looks rather like the opposite can be observed. The opposition appeared to believe that too high a level of consensus with the Social Democrat Government would risk being damaging to the opposition – even though they mainly agreed on the substantive issues.

When the proposal was discussed in the Standing Committee on Education (*Utbildningsutskottet*), requests were added for increased government payments to the schools. In the memorandum it was proposed, in addition to the extra government payment of 300 million kronor that were in the proposition, an additional payment each year of 50 million kronor for continuing instruction of teachers whose own education was old, for example teachers for grades 1-3.⁶⁹ The Standing Committee, with a majority consisting of the Social Democrats and the VPK (the Communist Party) also supported the VPK proposal. The Committee also emphasized that the municipalization must not bring with it the creation of regional or local differences, and suggested methods to penalize municipalities that did not fulfill the requirements. The requirements did not only specify the education per se, and related factors such as the density of teachers and the size of classes, but also educational materials, school buildings and rooms, school health care and school libraries. Persson (2007) highlights these issues as being central, and is of the opinion that the municipalities did not fully manage to fulfill their new responsibilities:

At the same time, I was fully aware that government direction of the school system would of course remain in the future. The curriculum, education of teachers and the continuing education of teachers were national government responsibilities, implemented by continual follow-ups and evaluations out in the field, in the municipally run schools. In 1991, when the Social Democrats lost the power of Government, the first part of the reform was implemented. The second part, concerning government follow-up and evaluation, was mismanaged by the new center-right Government. The new Minister of Education, Beatrice Ask, was too weak in her negotiations with the Association of Swedish Municipalities.⁷⁰

66 Persson 2007 p 54

67 Gennser interview 2007.

68 Pierre 1993 p 389 "*[S]ustaining the legitimacy of the public bureaucracy is basically a political – albeit not a partisan– issue* "

69 Here, the reference is to teachers that have been educated to teach grades 1-3, while in the new teacher education program that was introduced in 1988 educates teachers for grades 1-7.

70 Persson 2007 p 55. Persson does not, however, mention whether the Social Democrat Governments that were in power after 1994 did indeed remedy these claimed shortcomings or whether they, too, were too weak to prevail in negotiations with Association of Swedish Municipalities.

The criticisms from the Moderate Party were, however, primarily procedural in nature, and they were of the opinion that it was peculiar that such a far-reaching change as the municipalization of schools could be pushed through without more preparation. They also believed that the handling of the issue should have been overseen by the Parliamentary Committee on the Constitution. The Moderate Party, on this point, was supported by both the Center Party and the Liberal Party. The Liberal Party highlighted the problem that the issue had become a bone of contention in the union negotiations at the time, and that Parliament in this way had acquired a very odd role.⁷¹

The criticism from the Communist Party and the Liberal Party – contrary to that of the other parties – often addressed the reform as such. The former highlighted the risks that uniformity might be threatened and that the municipalization might lead to savings. The latter concentrated on criticisms from groups of teachers and were of the opinion that a reform that did not have union support should not be implemented, but they concurred with VPK's warnings that a municipalization might bring with it reduced resources to the schools. The Liberal Party line here can be contrasted with Gennser's, she was of the opinion that the most important goal of municipalization was to reduce the influence of a rigid teachers' union, and to create openings for changes in the activities.

The Social Democrat Government line of arguments was mainly based on that it would be to the schools' advantage that the teachers would have only one employer. The teachers' negotiating positions would be improved thereby, and salary negotiations made easier. The Cabinet also argued that decentralization would bring with it that the influence on the school activities from teachers, students, parents and other school personnel would increase.

As Gennser has pointed out, there was a wide-spread consensus between the national government and the municipalities, and also between Government and opposition in Parliament, that the then extant dual responsibility system had problems. The arguments brought forth by the teachers' unions was countered by the Social Democrat Government both with promises of clearer rules for goal fulfillment and increased funding, and with the argument that the municipal politicians, because of their proximity to the voters, would be forced to prioritize the schools in their budgets, to avoid losing voter support. The objections concerning differences between different localities or regions were met with that the national government would introduce far-reaching systems to follow up and evaluate. At the same time, from the center-right parties, there was criticism of the Minister of Education because he had, by his handling of the issue, contributed to the lengthening and deepening of the teacher conflict.⁷²

As previously mentioned, the Liberal Party warned that the reform could lead to savings. Lars Leijonborg, who was the Liberal Party spokesman on educational issues, wrote in a motion⁷³ as a response to the first of the propositions⁷⁴ from the Government on this issue that there were fears that the municipalization might

71 1989/90:Ub9

72 Bondelid & Kleist 1989

73 Motion 1989/90:Ub9

74 Proposition 1988/89:4

lead to savings – or at least a reduction in the rate of increase – for example by putting a larger number of students in the same class. Leijonborg referred to the Association of Swedish Municipalities that was of the opinion that the schools already were seen as too expensive. The motion in question, however, was more a criticism of how the municipalization was proposed to be implemented than against the change of responsible party as such.⁷⁵ It can be noted that Leijonborg used the high cost as an argument against municipalization, whereas Gennser and Persson saw municipalization to make schools more efficient, if not as a direct pretext to reduce the costs.⁷⁶ Ingvar Carlsson, however, objected to the actual description of the situation and questioned the statement that schools had high costs, as far-ranging savings had been made in the middle of the 1980s.⁷⁷ Gennser produces a picture that is in concordance with that from Leijonborg as to the process, and claims that there, across the entire political spectrum, was an insight that change was required and that the split responsibility must go, but at the same time, that municipalization must be accompanied by clear follow-up and inspection procedures to insure that the quality did not suffer.⁷⁸ Persson writes:

The center-right parties never wanted to undo the reform that I pushed through. The reason is simple. It is of course correct that the municipal employee, in this case the teacher, should have salaries that are set by the employer who sees them day to day.⁷⁹

Considering that the criticisms that were directed against the proposal when it first was presented were to a large extent about that the issue had been handled in a bad way, and were not criticisms against the proposal as such, it is hardly surprising that no serious attempts were made to re-transfer the schools to the national government.

In the magazine *SACO-magasinet* (*SACO* = Swedish Confederation of Professional Associations, an umbrella organization for unions organizing college graduates) fears was at the same time aired that local politicians would prioritize child care and elder care more than the schools.⁸⁰ Anitra Steen, the then under-secretary to Prime Minister Göran Persson, wrote in *Kommunaktuellt* (a magazine for and by Swedish counties and municipalities) that the municipalization would not mean that the municipal politicians would have more decision power, it was teachers, school principals and students who would acquire that.⁸¹ She also wrote that the municipal politicians would get influence over how the schools would be organized, and how the environment for the employees and the personnel policies should be improved.⁸²

75 Motion 1988/98:Ub5

76 Pierre 2003 p. 388 on the other hand, is of the opinion that the goal of the reforms were primarily to reduce costs. "First, they were to help facilitate cutback programs and to protect the Social Democrats from political embarrassment caused by public sector bureaucratization".

77 Carlsson, interview 2007

78 Gennser, interview 2007

79 Persson 2007 p 54

80 Ahlroos and Starnert 1990. In hindsight, it can be seen that they were wrong. The great pull-backs came in the domain of elder care, where a 20-year trend of increasing expenditures was broken in connection with that the tasks were municipalized. Lakomaa (2008)

81 Lindgren 1990

82 Lindgren 1990

SACO's chairman Jörgen Ullenhag was of the opinion that the decision had been handled incorrectly by first being brought in as part of the salary negotiations, then being moved out of the negotiations, and then again becoming part of the negotiation process. This had had as a consequence that SACO's salary negotiators had been switched from negotiating with the national government and the municipalities, back and forth and even at times in parallel.⁸³

The perception that Persson was a so-called *political entrepreneur* can be found in varying political camps. There was, with Persson, and with others, a fairly well established opinion that a municipalization would bring with it a possibility to break up positions that had previously been locked, and in particular be able to handle the issue of the influence of the teachers' union over the schools.⁸⁴ Persson's own experiences of the National Swedish Board of Education from the time when he was a municipal politician is said to have contributed to his interest in the issue. Persson himself writes nothing in his memoirs about his personal motives regarding this issue, but the National Swedish Board of Education was perceived by others as a rigid and bureaucratic authority which often interfered with the work of the municipalities.⁸⁵

Ingvar Carlsson is right that there were savings made within the educational domain during the 1980s if you view the cost per student. Between 1981 and 1982 the costs for the high-school level decreased, but as early as 1984 the costs were up to the same level as they had been in 1981, Even the costs for the grade school decreased during the same period, but only marginally. It is, however, doubtful whether Carsson's description of the trends is correct, because after the periods of decrease just described, the costs soon came to exceed earlier peak levels. During the period 1980 to 1989, the costs for the school system as a whole increased by 21 percent; the high-school costs increased by 28 percent and the grade school level costs by 12 percent.⁸⁶

The explanation for the higher costs is multi-faceted. Part of the explanation is that the number of students dropped. In 1980 the number of grade school students was 1,031,960, whereas the corresponding number for 1989 was 894,560. If no adjustments are made to the activities when the number of students decreases, the cost per student will rise. However, changing different school-related costs has varying degrees of difficulty. The costs for buildings and teachers can be hard to decrease even in the medium term, while the costs for – for example – educational materials and school lunches can be easily reduced if the number of students is decreased. Other factors that influence the costs are such things as the size of classes and teachers' salaries. During 1989 alone – that is in connection with the decision about municipalization – the costs for the high-school level increased by 18 percent; this can however be almost wholly explained by the large salary increases that were given to the teachers.

83 Ullenhag 1989

84 Gennser interview 2007, Berg interview 2007, Borg interview 2007, Åberg interview 2007

85 Carlsson interview 2007, Borg interview 2007.

86 SCB Statistiska meddelanden U12SM9101

The number of students at the high-school level increased during the same period, from 269,390 in 1980 to 289,580 students in 1989, which should have brought decreased cost per student.⁸⁷ During the period up to 1988 the cost per student – excepting the years 1982 and 1983 – were indeed largely constant. The costs for the various high-school programs did, however, vary significantly, which results in that the students' choices of programs has a strong influence on the resulting costs, and make comparisons more difficult. The costs for a student in the social science program (*samhällsvetenskapliga programmet*) are considerably lower than for a student in the program for agriculture, silviculture and horticulture (*naturbruksprogrammet*).

87 SCB Statistiska meddelanden U12SM9101.

7. Results of the Municipalization

The cost development within the school system can be analyzed in terms such as total cost, cost per student and cost as a fraction of public expenditure in general. The cost situation for the schools is influenced by a number of factors, where demographics are among those that are the most important.⁸⁸ Demographic changes can influence the cost situation for all three of these measures of cost, but the effects can become drastically different both for the same measure in the short and the long run, and for different measures of cost. Both teachers and students can for example be added and removed only at fixed intervals. A traditional classroom can only hold a certain number, and a teacher can normally only teach a certain number of students at the same time. This influences the cost development, both upwards and downwards.⁸⁹

As fraction of public consumption the expenditure for the schools shrank during the period 1975 to 1990. After this, the expenditures stabilized at a level just below 20 percent of total public consumption (see Diagram 3).

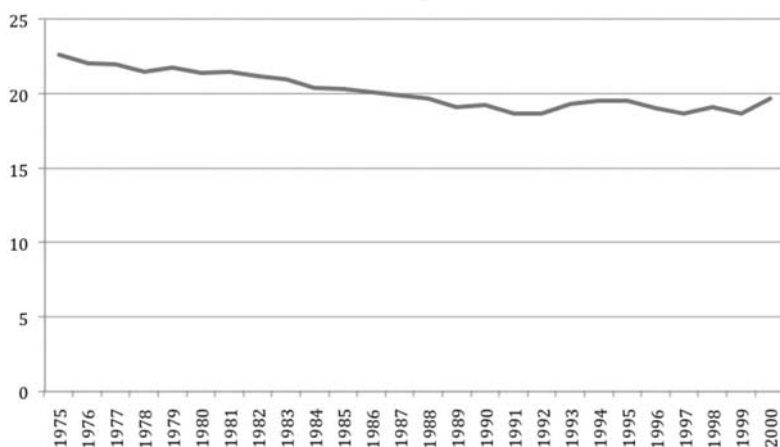


Diagram 3 Expenditure for the schools as a percentage of total public consumption. Source: SCB (Statistics Sweden)

⁸⁸ It would be plausible to assume that geography was an important variable, and that municipalities that are sparsely populated would have higher costs for the schools, for example as a consequence of a greater need for transportation to and from the schools. However, from a study of the statistics from the National Agency for Education (Nyckeltal för skolan) it is not possible to find any clear connection.

⁸⁹ The size of classrooms is usually the limiting factor. Few schools have classrooms that can accommodate more than a maximum of 32 students, and the marginal cost for one more student becomes very large, as it becomes necessary to use one more classroom and one more teacher. A reduction by one student, on the other hand, would not produce any savings of these types of expenditure. Naturally, the reverse is also true. If the number of students in the school described would go back to 32, a large saving would result, as the costs for teacher and venue could be cut in half. Many independent schools, partly to better manage variations in the number of students, have introduced new teaching methods where for example lessons in a traditional style are replaced by lectures and where the students do not have fixed places where they sit.

This picture is, however, illusory, as it is not caused by reduced costs for the school system, but by the fact that other parts of public activities grew more rapidly. As can be seen from Diagram 4, the cost per student increased markedly during the period in question, this at the same time as the number of students increased. Expressed in 1989 prices, the cost per student at the grade school level increased from about 30,000 to about 40,000 kronor per student per year between 1975 and 1989, and the cost per student at the high-school level from about 45,000 to almost 60,000 kronor per year. If you exclude 1989 when the costs increased substantially because of the increase in teachers' salaries, the situation for the high-schools becomes somewhat different, the cost then end up around 47,000 kronor per student, but for the grade school level the numbers are not significantly influenced by the salary increase.

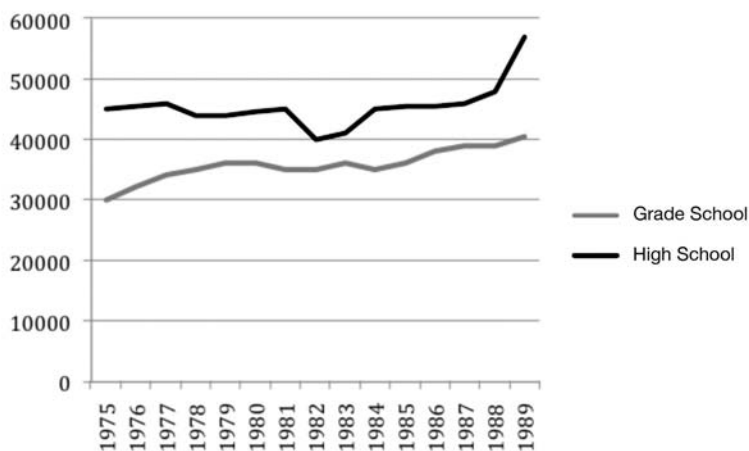


Diagram 4. Total cost per student at the grade school level and the high-school level, for the responsible level of government, 1975-1989, in SEK (Swedish kronor), 1989 prices. Source: SCB Statistiska meddelanden (statistical messages), U12SM9101

If we compare the cost development within the school system after the reform with other municipal expense domains, we find that the school costs first decrease somewhat during the period 1992-1996, and then very clearly increase (see Diagram 5). The explanation to this is probably partly to be found in that the municipalization took place at the same time as the crisis of the 1990s. The municipal expenditures for in principle all areas except social protection (that is welfare payments and the like) decreased during this period. The municipalities also were given an extra payment comprising about 350 million kronor in connection with the municipalization, but no trace of this extra money can be found when studying the cost development for the period that came immediately after the reform. The extra payment seems to instead have gone to other areas of municipal activity.

As fraction of all municipal expenditure, the expenditure for the schools has been unchanged since 1990.⁹⁰ The fraction in 1980 was the same as in 2000: 21.9

90 Statistiska Centralbyrån: Tidsserier för offentlig sektor 1993-2003

percent. The lowest fraction can be found in 1992 when it was 21.0 percent, and the highest in 1996 with 22.9 percent. Other changes that can be observed are that the cost fraction for health care has increased somewhat, from 25.1 percent in 1990 to 27.1 percent in 2000. The cost fraction for social protection (welfare payments and the like) is largely unchanged, but had a peak in connection with the economic crisis 1992-1993.⁹¹

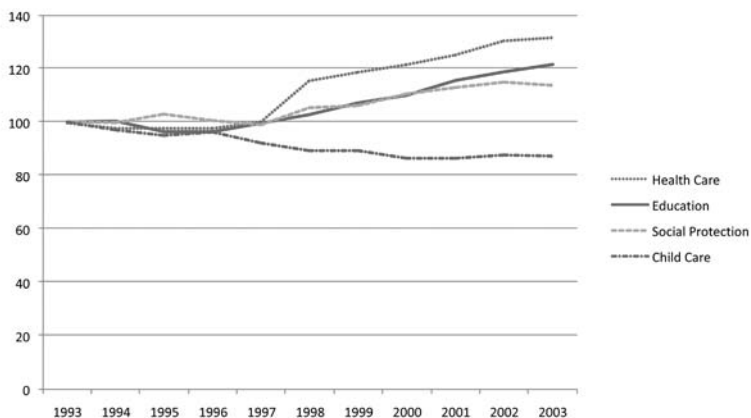


Diagram 5. Costs for municipal education (grade and high-school level), health care, child care and social protection, 1993-2003. Year 2000 prices, 1993=100. Source: Statistiska Centralbyrån: Tidsserier för offentlig sektor.

One factor that, however, does affect the cost structure and makes it hard to compare is that the cost for buildings was not fully accounted for before the municipalization. The cost for buildings was often charged to other accounts in the national budget, which risked causing a lack of overview and cost control.⁹² Further, according to Gennser, there was a big problem with deferred maintenance in many schools.

The current system for financing did not differentiate between whether the school was recently built or whether it came from the previous century. This gave absurd results.⁹³

If Gennser's surmise is correct, it can be assumed that the costs would have increased as a consequence of this dammed-up need for maintenance even if the national government had stayed on as the responsible party. From this standpoint, it is difficult to say how the cost situation developed in connection with the municipalization, but it should be possible to see a break in the trend by comparing longer periods before and after the reform.

It can also be noted (see Diagram 6) that the cost per student leveled out and then increased marginally after the municipalization, except in those municipali-

91 Statistiska Centralbyrån: Tidsserier för offentlig sektor 1993-2003

92 Gennser, interview 2007

93 Gennser, interview 2007

ties that were absolutely the most expensive. The cost per student and year has, in those cases, remained at the level where it was when the municipality took over the responsibility, or has dropped somewhat. The largest cost increases have at the same time taken place in the 10 percent of municipalities which had the lowest costs for their schools. The large difference, however, is in the handful of municipalities which, before the municipalization had considerably higher costs than the rest, which have subsequently reduced their costs.⁹⁴ The difference between the ninth decile and the municipality with the highest costs was in 1991 close to 40 percent, and that number decreased to about 20 percent by the year 2000. Those who claim that the municipalization brought with it reduced resources thus are correct only with regard to the municipalities that have the highest costs. In other municipalities, the resources have increased or been unchanged.

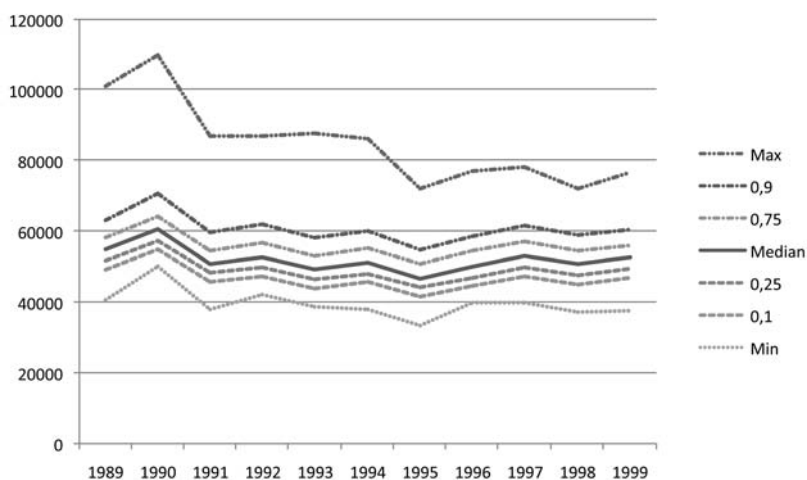


Diagram 6. Cost per student (for the responsible party) in grade schools, year 2000 prices. Source: National Agency for Education, National Swedish Board of Education⁹⁵

During the period studied, a school voucher system was also introduced, and thus government subsidies to independent schools. This is something that will not be discussed in this paper, but it may be worth noting that the competition from the independent schools does not seem to have brought with it any pressure to make the school system as a whole more economically efficient. During the first system with independent schools, those schools received a simple payment corresponding to 85 percent of the cost per student in the municipal schools. Thus, there was a possibility for savings for the municipalities. The number of independent schools compared to the total number of schools was however small during this period so the effect must be assumed to have been very limited indeed. Under the new system of payments which was decided upon in 1996, on the other hand,

94 The municipalities with the highest costs for schools were usually Kalix, Övertorneå, Jokkmokk and Ragunda, all in the Northern and sparsely populated part of the country.

95 Because of a change in how the calculations were made, as well as in which municipalities participated, the numbers are not fully comparable to those in Diagram 4.

there is no such possibility for savings as this system is based on the independent schools being paid on the same basis as the municipal schools.

As the choice of high school program had – and still has – a large influence on the costs for the high school level, it is considerably more difficult to make comparisons in this area than for the grade school level where the choices of the students do not impact the cost structure to any significant degree. The costs for a student in the program for agriculture, silviculture and horticulture can for example be ten times higher than the costs for a student in the social science program. The offerings and availability in each municipality and the students’ choices thus gain large importance and it is therefore not meaningful to make the same comparisons between municipalities as have been done for the grade school level. On the other hand, it can be noted that the average cost for the high school level first decreased after the municipalization, and then increased. The point where the trend shifts does, however, coincide with the introduction of the “new high school” where the “lines” of study were replaced with “programs of study” and where the previously two-year educations became three-year educations.

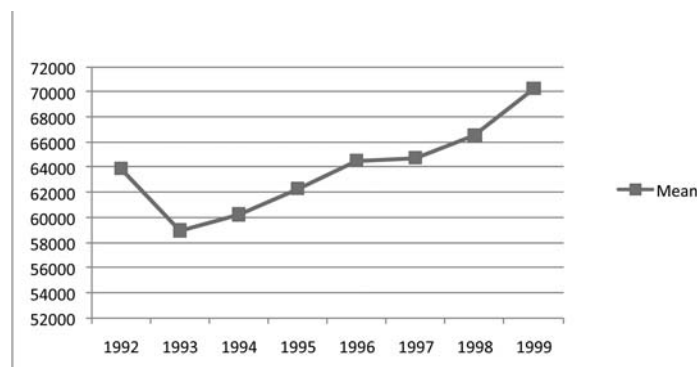


Diagram 7. Average yearly cost per student at the high school level. Swedish kronor, Year 1998 prices. Source: National Agency for Education (Nyckeltal för skolan) 1992-1999.

The trend is nevertheless clear. Regardless of whether the measure is the proportion of school costs as a fraction of total public consumption, as a fraction of municipal consumption or cost per student, there is a break in the cost development curve in connection with the reform. The decision to implement the reform was followed by a substantial increase in the teachers’ salaries, but starting the year after the decision, the costs leveled out. That the decision impacted the school costs is therefore clear. The clearest results come from the municipalities that before the reform had the highest costs for the grade schools.

Concerning the fears that the municipalization of schools would produce increased differences between different municipalities and regions regarding the amount of resources that are targeting schools, it can be observed that this did not happen. Rather, the differences between high cost and low cost municipalities have been somewhat reduced, mainly by that those municipalities that had the highest costs before the reform have reduced their costs.

8. Explanatory Approaches

The questions concerning the transfer of the schools to the municipalities ("municipalization") that are of special interest for further investigation are (i) why the process up to making the decision was so drawn-out despite the fact that the actors, at least as to what the problem was and what the solution was, were in agreement in principle. There was, for example, most likely a Parliamentary majority for municipalizing the schools all the way back to the early 1970s, and (ii) why the municipalization broke the trend of ever escalating costs. Several theories can be employed to answer these questions.

No theory can likely be said to totally explain all the actions of the decision makers involved, or why the reform did get the outcome that it did. Rather, it is the case that political decision making is a difficult area to research because so many factors are in play. It should also be noted that this paper is not about testing whether certain theories are correct or not. The ambition is to instead to see whether any of the predictions made by the theories fit the actual outcome (naturally, this should not be taken as *prima facie* proof that it was these particular psychological effects that created the outcome), and to see whether the decision makers themselves may have considered these effects when they acted to push through the decision or when they shaped the reform.

There are a large number of theories within economic psychology that potentially could be applicable to the municipalization of the schools. Additionally, there are theories within Political Science and within historical research that can be applicable to varying extents. This, too, will be studied later in this paper.

8.1 Economic-psychological theories

The classical rational decision model has been challenged by researchers in economic psychology. These researchers have observed that people's behavior deviates from that of theories about rational behavior in economic sciences. A central theme has been negative deviations such as that people do not always maximize the long-term benefit when they make a decision, but instead are governed by short-term considerations, by psychologically easily accessible information and by their emotions. Economic-psychological theories are also used to explain how people solve conflicts. It should be noted that this paper does not try to test whether these theories are correct. The ambition is instead to see if any of the predictions that these theories give do indeed match the actual outcome, and also, if possible, to see whether the decision makers themselves may have considered these effects when they have worked on getting any particular decision accepted by Parliament or when they shaped the reform.

The economic-psychological theories that are used in this paper can be sorted into four main categories: *reference point theories* (adaptation level), *mental accounting*, *the prospect theory and Proximity Effects* (social impact theory). These can be said to constitute the fundamental concepts within economic-psychological theory (Belsky & Gilovich 1999).

8.1.1 Mental Accounting

Mental accounting means that people divide current and future resources (money) into different (explicit or implicit) accounts depending on their origin, when they will be used and for what purpose. Through this method, gains and losses will be experienced differently depending on which account they impact, and this influences consumption decisions (Thaler 1980, 1985, Kahneman, Knetsch & Thaler 1991). The propensity to save versus to consume differs between different mental accounts. For example, the propensity for saving is large for capital accounts and for lump sums, but small for income and consumption accounts (Thaler 1980).

Thaler (1985) exemplifies with a couple that has saved 15 000 dollars to be able to, five years later, buy a vacation cottage. The money exists in an account that produces 10 percent interest per annum. At the same time, they buy a car for 11 000 dollars which they finance with a three-year car loan running at 15 percent interest per annum. The money in the savings account and the money from the car loan are found in different mental accounts and are evaluated separately, so instead of using the money from the savings account to buy the car, they borrow money at a higher interest rate than the yield on the savings account.

Mental accounting can have different effects depending on how the accounts are defined and how they are combined. If we have two outcomes, x and y , and evaluate them together as one account, that is according to the formula $v(x+y)$, i.e. $v(x)+v(y)$, this is defined as being “integrated”. If, on the other hand, we evaluate them separately, this is defined as being “segregated” (Antonides 1991). If both outcomes (x) and (y) are positive, segregation will produce a higher total value, because the evaluation function is concave. “*The moral of this is not to wrap all Christmas presents together*” (Antonides 1991). If, on the other hand, both outcomes are negative, integration should be used because the total disutility is then lower. This phenomenon could for example be what is behind that many people tend to spend more when they pay by credit card than when they pay cash. Since the credit card bill adds many small expenses into one large one, the experienced loss is reduced by the integration of the accounts, at the same time that the utility of the different purchases remain segregated.

Another case is when one outcome is positive and the other is negative, but their sum is positive. Integration then results in the negative outcome being extinguished by the positive outcome, and the result is viewed as a gain. For example, this can explain why taxation at the source (as in payroll deductions) produces less dissatisfaction than if the taxes have to be paid by the taxpayer. The payroll deduction system makes the income and tax accounts integrated. If, on the other hand, the situation is one where one outcome is positive and the other is negative, but where the sum is negative, it is not obvious whether integration or segregation will be used. If one outcome, x , is small compared to the other, y , a so-called silver lining effect can materialize by segregating the accounts. Silver lining means that some of the suffering that a bad outcome produces is mitigated by the happiness that is given by the positive outcome. Thaler (1985) shows with an example how this might work.

Mr. A's car was damaged in a parking lot. He had to spend \$200 to repair the damage. The same day the car was damaged, he won \$25 in the office football pool.

Mr. B's car was damaged in a parking lot. He had to spend \$175 to repair the damage.

Who was more upset?⁹⁶

When the question was posed to students in an experiment, 19 answered A and 63 answered B, while 5 saw no difference. In this case, there was clearly a silver lining effect. The same effect can be used in a business context, for example when the seller gives a discount. The discount is often small compared to the price, but is used to reduce the suffering of having to spend money. Mental accounting is connected to several different psychological phenomena which concern human decision-making, among which are status-quo effects or endowment effects, omission bias and sunk cost effects.

The endowment effect means that people tend to over-value things they have (but might lose) and undervalue things they do not have (but can obtain). Thaler (1980) gives an example: Mr. R in the late 1950s, bought a case of good wine for five dollars a bottle. A few years later, the wine merchant offered to buy back the wine for 100 dollars a bottle. R refused, in spite of the fact that he never had paid more than 35 dollars for a bottle of wine. If he instead had been offered a choice between 100 dollars and a bottle of this wine, we may assume that he would have chosen the money, as he never had paid more than 35 dollars for a bottle of wine. By the fact that he already owned the bottle, he was not willing to give it up even if he would not have bought it at that price.

Kahneman, Knetch and Thaler (1990) performed a classic test of this effect by showing that people who randomly had been given a mug demanded a significantly larger payment to sell their mugs than those who also randomly had been chosen were willing to pay to buy the mugs in question. Samuelson and Zeckhauser (1998) call the same effect a status-quo effect as it means that status quo is preferred to alternatives that consist of change.

Omission bias means that the decision maker prefers an alternative that requires no action to one that does require action; the result is the same as for the status-quo effect. A test for this effect was performed by Hartman, Doane and Woo (1991) and used electric power customers in California. The customers were asked how they would consider different combinations of service and prices where some combinations were said to be the status quo. Regardless of whether it was a combination of a low price and little service or a high price and lots of service, most people chose not to change (see also Kahneman, Knetsch & Thaler, 1991). Omission bias can also be connected to the fear of being held responsible. He who actively chooses to do something is much more likely to be held responsible than somebody who passively watches and lets things happen. A classic political example is the argument against seeding hurricanes.⁹⁷ Even if the total amount of damage would be

96 Thaler 1985, p 204

97 By airdropping chemicals from airplanes, it is possible to produce rain, and thereby make for example hurricanes use up their energy content earlier and change their paths and thus

less if the hurricane was seeded, it would be possible to hold somebody responsible for the actions that led to the damages. Potentially, somebody can be sued for the damages that occur by a hurricane changing directions caused by seeding whereas a hurricane that follows its natural path is act of God. It is possible to argue in terms of that damages caused by acts of omission are seen as foregone gains, whereas damages caused by acts of commission are not. Kahneman and Miller (1986) have also shown that acts of commission produce a larger amount of regret than acts of omission if the outcome is negative. Another observation is that the willingness to pay for the removal of an existing risk is often less than the willingness to pay for not having to accept a new risk. Omission bias can also be present in decision situations where the outcome of the alternative not chosen will never be known. For example, people can be unwilling to vaccinate their children even though the risk of death from the vaccine is lower than the risk of death from the disease against which the vaccine would have offered protection (Ritov & Baron 1990).

The *sunk cost effect* means that we base decisions on other decisions previously made and not on the consequences of the decision we are facing. Thaler (1980) explained the sunk cost effect with loss aversion, combined with integration of mental accounts. If you have already spent nine million on an investment, you might as well spend another million to get something. The extra million is then put in relation to the outcome of the whole project, and can be seen as reasonable, even if the value of the whole project does not reach ten million (but is more than one million). If you do not put in the extra million, you will experience the nine million already spent as lost, which you want to avoid in spite of the fact that an alternative use of the last million could have given a higher payback.

The sunk cost effect can also be explained with “regret”, as according to Arkes and Blumer (1985). We feel more regret if we invested nine million and got nothing back than if we invested yet another million and received something. They also describe how the prospect theory predicts that people take risks in a bad situation, with the goal of regaining earlier losses or to regain sunk costs. Sunk costs can also influence decision making through “escalating commitments” (Staw 1976, Schaubroeck & Davis 1994, McDermott 2004).

Individuals who are not responsible for an original policy that failed may be more likely to stop the policy, as opposed to putting further resources into it. Those responsible for the policy appear to want to recoup their losses through an escalations strategy and to recover their sunk costs from the previous effort more than outsiders do.⁹⁸

Both the sunk cost effect and the omission bias produce what in economic history is usually called *path dependencies*: that is we continue on the path begun, because earlier events and decisions limit the alternatives between which to decide today. Network externalities are a common rational explanation to path dependencies, the ratchet effect is another. *Network externalities* have been described above and ratchet effects are a political science based explanatory approach which describes that some decisions become politically irreversible. For

hit areas that are less populated
98 McDermott 2004, p 300f

example, it can be much harder to raise speed limits once they have been lowered than to stop a lowering, however small. Those who want to raise the limit will immediately be accused of wanting to increase the number of traffic fatalities. The reasons for the irreversibility can be different factors, including psychological phenomena such as reference points or omission bias. The latter because whoever makes the decision would risk being held responsible – at least indirectly – whereas the gains from the increased limit would not be traced to any one individual decision maker.

8.1.2 Reference Points

In decision situations, reference points have an important role. How we value some things depends on which reference point (within a mental account) that we use. This can express itself in different ways. According to the classical Weber-Fechner model, the intensity of a sensation is proportional to the logarithm of the intensity or the strength of the stimulus that causes the sensation. This means that we will react more strongly to for example an increase in the price of an item from 10 to 20 than from 20 to 30, in spite of the fact that in the latter case we will have less money left after the purchase (Gunnarsson, Wahlund & Flink 2000). Another variant is adaptation level or context effects (Helson 1964). This means that our subjective judgments are relative to the level that we are used to. We would for example perceive a tennis ball that weighed 4 ounces as heavy, but a football weighing 4 ounces as light.

By defining these reference points, different results can be achieved. This is commonly called “framing”. The use of “cash discounts” or “credit card surcharges” in stores means that the merchandise has two different prices, one if you pay cash, another if you pay by credit card (Thaler 1980). The customers experience the presence of a cash discount as a gain, whereas they experience the credit card surcharge as a loss. Because the value function is steeper for losses than for gains, the customers will, however, be more likely to use credit cards if they perceive it as foregoing a cash discount (that is forgoing a gain) than if they perceive it as that they pay a credit card surcharge (that is accept a loss). If the merchant gains more by his customers paying by credit card, he will thus call the difference a “cash discount” and vice versa. The importance of framing also means that the setters of agenda and political entrepreneurs have an important role as they can decide how the alternatives are presented and they can therefore position them in different ways on the value function depending on what they want to achieve.

8.1.3 Prospect Theory

Prospect Theory (Kahneman & Tversky 1979) is based on the fact that people care more about changes (within mental or actual accounts) than about totals, levels or states, and prospect theory describe how people make decisions in situations that include risk and how they value potential gains and losses. According to Prospect Theory, the value function is concave for gains and convex for losses. This leads to loss aversion for gains and risk seeking for losses. Additionally, the value function is in itself loss averse, that is the function is steeper for losses than for gains.⁹⁹

The implications of this theory is for one thing that people pay more attention to losses than to gains, and for another that change is more important than level or state. The latter phenomenon is because there is a tendency to define changes as disimprovements. Experiments have also shown that changes that are near to the reference point are assigned a bigger weight than changes that are further away from it. Additionally, there is a tendency for people to overestimate small probabilities at the same time that large ones are underestimated (Kahneman & Tversky 1984). Experiments show, for example, that people overestimate the risk of dying in air plane crashes, but underestimate the risk of dying as a result of diabetes (Slovic 2000). According to Wahlund (1994) small probabilities are overestimated more strongly in situations of potential loss than in situations of potential gain. This can be assumed to result in that a change becomes difficult to implement because negative outcomes from the change will get more weight. All this affects how people act in decision situations.

Bazerman and Neale (1991) have described how Prospect Theory affects negotiations. If negotiator A believes that each concession he makes is a loss to him or to the interests that he represents, this will result in that the probability of achieving an agreement is less than if the negotiator believes that each concession made by the other party, negotiator B, is a gain for A: *"Negotiators bargaining over losses tend to make fewer concessions, find fewer integrative solutions, and more often fail to reach agreement than negotiators bargaining over gains."*¹⁰⁰

It follows from Prospect Theory that the concessions that give the most effect in a negotiation are those that reduces the other party's losses, whereas the least effective ones are those that increase his gains when he is already ahead.

Reference points and the value function according to Prospect Theory also affect how differences between different alternatives are evaluated. The difference between disadvantages tends to have more weight than differences between advantages. Kahneman (1992) describes for example how the difference between two salary offers of 40,000 and 45,000 dollars will be perceived as the difference between two gains by somebody whose present salary 35,000 dollars, and as the difference between two losses by somebody whose present salary is 50,000 dollars. As

⁹⁹ That people are more sensitive to losses is, however, nothing new, but something that was noted as early as by Adam Smith who in 1759 wrote "We suffer more [...] when we fall from a better to a worse situation, than we enjoy when we rise from a worse to a better" (Smith, 1759 p 311).

¹⁰⁰ Kahneman 1992, p 297

the value function is steeper for losses, the difference between the two alternatives will be perceived as larger for the person with a high salary than for him who has a low salary.

8.1.4 Proximity Effects

Another important field within economic psychology is something we can call Proximity Effects. Proximity Effects mean that the decision maker pays more attention to people whom they meet or risk meeting than to people that they will never have to meet when they make a decision. Proximity Effects have been described by Milgram (1963) and by Kilham and Mann (1974), among others. A special field is Social Impact theory (Latané 1991). Experiments done by Latané show, for example, that it is easier to influence somebody in a small group than in a large one, that is we pay more heed to what others have to say in a smaller setting, and that we contribute more in such a smaller setting. Latané showed, among other things, that a group that has eaten at a restaurant gives more tips if they get one check per person than if they get one check for the whole group, and that there were more people who became convinced by the evangelist Billy Graham if they listened to him in a setting with few other listeners (Latané 1981, Latané & Wolf 1981).¹⁰¹ Applied to political decision making, this can explain why more consideration of the voters is given at a low administrative level, such as the municipal level, than at the county or national level. This is a well-known phenomenon in politics. Myrdal (1982) reflects that it was harder to make decisions when he was the Mayor of Mariefred than when he was a Member of Parliament, because in the former case he was at a considerable risk of running into somebody who had been affected negatively by the decision.¹⁰² Even Gunnar Sträng supposedly has thought in terms of Proximity Effects when he pointed out that municipal politicians – in contradistinction to politicians and civil service employees at the Ministry of Finance – often had a hard time standing up against demands from the voters.¹⁰³

101 It can be noted here that the examples described can also be explained by mental accounting in combination with different reference points. The restaurant customers put the tip and the cost of the food in different mental accounts, and they experience it as leaving a bigger tip if the tip as an absolute number is larger. This gives the same result as the proximity effect. This, in turn, can serve as an example of the fact that it is often difficult to isolate which effect that is behind which; this admonishes us to be careful about drawing conclusions.

102 Myrdal 1982 p 86

103 Åberg, interview 2007

9. Analysis

The phenomenon that politicians most often refer to themselves – directly or indirectly – is the proximity effect. Politicians seem to be aware that it is often harder to make a decision that is disadvantageous to a person if the person affected is a person that the decision maker runs a risk of running into – face to face. According to Åberg, the then Minister of Finance, Gunnar Sträng, tried, for this reason, to prevent his subordinates from having too much contact with municipal politicians throughout the country. These contacts he wanted to handle himself. If you let the municipal politicians govern the process, the costs would run way up, according to Sträng:¹⁰⁴ *“In the bunker that was the Ministry of Finance, it was easier to stand up against such demands.”*¹⁰⁵ Gennser also is of the opinion that politicians at a lower level often are more sensitive when it comes to making decisions that negatively impact voters, and refers to the decentralized Switzerland.¹⁰⁶ The connection between the level at which a decision is made and the size of the public sector has been the object of extensive research, primarily within the Public Choice tradition, a school of thought to which Gennser also refers (Gennser 1982).¹⁰⁷

Considering that politicians with different backgrounds are of the opinion that the proximity effect matters when it comes to which decisions are made, it is interesting to investigate if any part of the outcome of the municipalization of the schools can be derived from the proximity effect. If we start with Sträng’s assumption, we would expect that the transfer of the responsibility for the schools would bring with it that the costs would increase, as a consequence of that the municipal politicians had a harder time than the national government to stand up against demands, for example from teachers, to get more resources. These predictions from the proximity effect can, however, have been counterbalanced by other proximity effect-related factors. One of the demands that the citizens of a municipality make to the municipal politicians can be that they should economize with resources and not use them in a way that is obviously wasteful. This demand too should, according to the proximity effect, be harder to stand up to for those closest to the people affected by the decision. Additionally, there are other factors that may have contributed to strengthen this process. One such effect is that by decentralizing the responsibility for the schools, it became possible to make comparisons between municipalities in a way that had not been done previously. Even if much of the activities of the schools was strictly regulated by the national government, there was room for a certain amount of experimentation, particularly in areas not directly connected with instruction, such as the buildings and school meals.¹⁰⁸ The municipi-

104 Åberg, interview 2007

105 Åberg, interview 2007

106 Gennser interview 2007

107 For an overview, see Mueller 2003, pp 209-229

108 There are excellent statistics on the different areas of expenditure for the schools, available from the National Agency for Education. Unfortunately, the statistics cover only the period after the reform; to investigate the changes that are discussed in this paper, they are of modest value. On the other hand, the statistics constitute a great foundation for anyone who wants to study how individual municipalities have handled the new responsibility for the schools. One problem with all cost comparisons within the public sphere is that it is hard to measure quality. Since 1997 (regulation 1997:702 concerning accounting for quality within the school system etc.) all schools must make an annual accounting for quality, in

palization brought with it that it was possible to point to successful and less successful municipalities, and to make demands to the politicians to imitate successful efforts and avoid those that had proven unsuccessful. Another factor that may have contributed to strengthening the demands for avoiding waste is that problems at the municipal level is often subject to closer scrutiny by the media.

Economic mismanagement in a municipality has a higher risk of being brought to attention by the local press than in national media, and the proximity effect also renders the municipal politicians more sensitive to such criticism. During the period that the schools were run by the national government, the distance was large between those that were influenced by the decisions and those who were responsible for them, and it might thus be thought that it was easier to ignore criticism that pertained to individual municipalities or schools during that period than after the municipalization.

The clearest result of the municipalization was that the costs in the handful of municipalities that had the very highest costs when the reform was implemented ended up being seriously reduced. The costs for schools in other municipalities, on the other hand, were at the same time constant or increased very moderately. This should be explained the proximity effect in combination with changing reference points. The more successful municipalities become the new reference points and the proximity effect can proved explanation to why the municipal politicians cared about it.

At the same time, the municipalization brought with it that it became necessary to calculate just how much the schools did cost, and that costs and potential possibilities for savings thus became visible. Even the transfer by itself from the national to the municipal level can have sparked savings as a consequence of mental accounting effects and by changes in reference points. Expenses that, while the schools were a national responsibility, were not perceived as too large, may have come to seem that way when the same costs had to be paid by the municipalities. When the whole of the National Budget, or the whole of the National Budget for schools, was the reference point, certain of the expenses in some areas may have been perceived as insignificant. These areas of expenditure can, on the other hand, have been perceived as large when the reference point instead was that of the school budget for an individual municipality.

writing. The National Agency for Education lists, in its general advice (Skolverket 2006 pp 22-23) a number of factors that ought to be part of the quality accounting. Included therein are, among other things, *“availability and quality concerning educational material, materiel, equipment and school library [...] conditions concerning the work organization and the governing organization [...] the work on learning and education [...] development of leadership and the development of competency of the personnel [...] the work following up how much the students learn, and individual development programs, study plans and intervention programs, and with setting of grades for knowledge, for older students [...]. The fulfillment of goals concerning the goal of the study plans for norms and values.”* There are thus no accepted general quality measures for the schools that could be compared with the costs to obtain some measure of effectiveness. The weighting of different factors that the National Agency for Education use as constituting quality is clearly subjective and as each school produces the quality accounting of itself it would have little meaning to compare the quality measures for different schools. As a measure of how the quality of individual schools varies over time, they might, however, be useful.

When evaluating the actual cost development after the reform, it should be considered that several high-school programs, during the period studied, were extended from being two-year programs to being three-year programs. This should have brought with it a general increase in costs. Of course, it is difficult to allow for this cost, as the extension of the two-year programs may have changed the patterns of demand for the different programs, but it is possible to assume that the result in any case would not have been a cost reduction for the schools. This makes the break in the cost development curve brought on by the municipalization even more evident.¹⁰⁹

Another important psychological factor that may contribute to explaining the results of the municipalization is that the transfer of responsibility brought with it a change of mental accounts and that previously locked positions caused by endowment and status quo effects were unlocked. For example, Lars-Eric Ericsson presented this as one of the main reasons why the Association of Swedish Municipalities wanted to municipalize elder care.¹¹⁰ As long as the counties were the responsible parties “it was impossible to make any kind of change.”¹¹¹ It can be plausibly imagined that the same was true concerning the municipalization of the schools. When an activity is moved, this can be seen as rebuilding the system from the ground up without being locked into how it was done earlier. The new system is framed in a different way which makes it possible to make large changes without those impacted becoming needlessly opposed. Åberg is of the opinion that within the Ministry of Finance, as early as the early 1970s, there was an understanding that it might work this way, but that this did not affect the policies promoted. “*They were simply not that strategic in their thinking.*”¹¹² Ingvar Carlsson (2007) confirms Åberg’s description but emphasizes that there were no economic considerations behind the reform.¹¹³ Obviously, it is impossible to determine if there were any hidden intentions, but the fact that at least the Government wanted to avoid giving

109 The school voucher reform does not seem to have had any noticeable effect on these results, most likely because of the fact that the number of voucher-financed non-government schools was very small during the first part of the voucher period, when those schools received 85 percent of the money per student that the municipal schools received, and that the system was changed to that the non-government schools in principle received the same amount as the municipal schools during the later period, when the number of non-government schools started to increase. The non-government schools can thus be assumed to have brought with them neither higher nor lower costs. Possibly, the competition from non-governmental schools may have improved the employment conditions for the teachers by offering alternative employers. This does not, however, appear to have any effect on driving up costs, except indirectly, as the salaries in the non-government schools on average are lower than in the municipal schools. Here, it is possible to speculate as to whether this was balanced by a better work environment and better non-monetary benefits at the non-government schools than in the municipal schools, which in turn may have been forced to compensate with higher salaries. This is an issue that is, however, not studied in this paper. It can, however, be noted that the productivity in the public sector increased rapidly in the 1990s, something that could be attributed to competition.

110 Ericsson, interview 2007

111 Ericsson, interview 2007

112 Åberg, interview 2007

113 Neither Carlsson, Borg nor Åberg were of the opinion that there were any consideration given to that the salary costs – because of the lower productivity in the public sector – would lead to ever increasing costs for the labor-intensive parts of public activities. Berg 2007 believed that there was probably an awareness of the problem within the Ministry of Finance, but that this did not have any effect on policy.

the impression that they expected the municipalization to result in different developments in different municipalities in any case indicates that the Government did not try to use this as an argument for change. Instead, the Government emphasized that the municipalization would result in increased uniformity because of the new mechanisms for control that were introduced. Other actors, not leastly the municipal politicians, may however have seen municipalization as a way to break old patterns.

Not just the outcome of municipalization but also the process that lead up to the decision can be analyzed with a starting point in economic-psychological theories. For example, using the theories of loss aversion and mental accounting, we can give an explanation for why political changes are combined with additional funding as bait. This would not have been needed in a world of neo-classical actors, where a change in responsible party in principle would have been an accounting issue. The action was one of moving both responsibility and financing from one political level to another. At the municipalization of the schools, additional funding was doled out to overcome the resistance to change. As the most wide-spread opposition against municipalization came not from within Parliament but from the teachers' unions, the compensation was primarily in the form of significant salary increases to the teachers that were members of *TCO* (Swedish Confederation of Professional Employees, a white collar union).¹¹⁴ In connection with the reform, there was also extra funding made available for furthering the education of the teachers, as an extra carrot to induce them to accept a change.

Economic psychology can also contribute to an increase in the understanding of why the process became so drawn-out. As early as in connection with the finalization of the transfer of schools to the national level in the early 1970s, there were discussions about a re-municipalization. At that time, even the teachers' unions were supportive of a municipalization.¹¹⁵ The fact that the schools had just been transferred to the national level most likely made it more difficult to immediately reverse that change. A reversal was also made more difficult because the transfer to the national level had been made gradually during a long period. As a consequence, when the schools in the last municipalities were brought to the national level 1972-73, the situation was that, for many, the schools as a national responsibility was already an established fact and for those people this constituted the reference point. Thus, there was already a large group for whom municipalization would be perceived as a loss, and this group can thus be assumed to have been disinclined to change. As the reference point had been moved, that which had earlier been the norm came to be perceived as risky. The established order, status quo, was regarded as the safe alternative and anyone who wanted a change had the burden of proof.

As both the municipalities and the national government wanted to implement the reform, it was not primarily a battle between different political levels, as was the case with the concurrent *Ädel Reform* where municipal and county interests

114 Even the Liberal Party – which was the only party in Parliament that opposed the reform for reasons other than those concerning the decision process – brought out the opposition from the teachers as the primary reason to say no to the municipalization.

115 Carlsson, interview 2007

were opposing each other. Instead, it was mostly a problem of getting the teachers' unions to accept the municipalization. As the teachers, as a consequence of the concurrent salary negotiations and the strike received substantial salary increases, this resistance was broken.

That the salary increases came in connection with the decision about municipalization most likely contributed to the fact that the resistance from the teachers' unions faded away. As the two changes, the salary increases and the municipalization, coincided in time it was easier for the teachers to integrate the two accounts. The part that the teachers viewed as a loss, the municipalization of their positions, was thereby extinguished by the gain through salary increases. If the issues had been handled as two separate decisions, it is likely that it had been less simple. Then, the two accounts would have been evaluated in a segregated manner, and the resistance from the teachers would then likely have been greater. From this perspective, the way the Government handled the issue was very skillful. If the decision had been delayed, it would have been more difficult to make this connection.

If alternative models from political science, such as Cohen, March and Olsen's (1972) or Kingdon (1995) are applied, the result is that they predict that the decision would either have been made as soon as the issue came up, or the decision would never have been made. The model of Cohen, March and Olsen can be briefly described as that a given solution searches for a problem to solve. In this case however, both the problem (split responsibility) and the solution (the transfer of responsibility to the municipalities) were given from the beginning. No other problems or solutions had been discussed. On the other hand, Kingdon's model describes how decisions can be made only when there is a window of opportunity. These windows are often created by external events. An airplane crash can open a window for increasing the safety standards for aviation, changes that would not have been possible otherwise. Such an external event did not occur within the school system, and the window of opportunity was in the case of the schools open from the early 1970s and onward, or else shut the whole time. Thus, the decision should have been made immediately or not at all. If, on the other hand, this theory is connected to the above analysis of how the teachers' handling of mental accounts worked, such a window of opportunity can be found – that is the then ongoing teacher strike that facilitated a connection between the municipalization and the salary increases. Here, it is the insights from economic psychology that make Kingdon's model useful.

Several of the key actors, for example Carlsson, Gennser, Borg and Ericsson, are of the opinion that the appointment of Göran Persson as Minister of Education was the deciding factor for the decision about municipalization to be made. Persson's own experience as a municipal politician made him more eager to do something about the problem of double responsibility and Borg claimed that Persson's own experience of the National Swedish Board of Education (*SÖ*) interfering with the activities caused him to be eager to drive through a reform that would have as a re-

sult that the power of *SÖ* was limited.¹¹⁶ In Kingdon's sense, the accession of a new political actor does not constitute a window of opportunity; rather, Persson should be seen as a political entrepreneur. At the same time, the municipalization was not Persson's idea. Prime Minister Carlsson had appointed him as Minister of Education with a clear mandate to change.¹¹⁷ The appointment of Persson can thus be seen rather as a result of the fact that a decision to change was underway than as a precipitating factor. However, it is likely that Persson had a decisive role when it came to handling the criticism of the municipalization from the unions.¹¹⁸

The Rational Choice models (Arrow 1968, Elster 1986) also give the same predictions as Cohen, Marchand Olsen and Kingdon as there were no differences of opinion regarding neither problem description nor solution. Nor had anything fundamental changed during the almost two decades from when the issue was first discussed to when the decision was made, so the probability of the decision going through would have been the same in 1971 when the issue was first raised as in 1989 when the decision was finally made. It should also be noted that Kingdon's explanation model, as does Borg's (2004), are about issues when there is political dissention and where there are two or more alternatives from which to choose, which was not the case here.

Nor can institutional theory explain why the decision was made. In this case, the institutional changes were made after the decision about municipalization. It had been quite possible to for example introduce the school voucher system in spite of the fact that the schools had remained a responsibility of the national government, or to municipalize the school without reorganizing high school education.¹¹⁹ Obviously, actors can try to change the institutions to their own advantage or anticipate which institutions are about to be changed and act accordingly. However, here it is very unclear which changes were on the way and which actors might have benefited from the changes. On the other hand, Institutional Theories can contribute to the explanation for why the transfer of responsibility also produced changes in the cost structure. The new institutional framework which was introduced by the reform did differ from the one which had previously been in place, and this can have influenced how different parts of the activities were valued. For example, it can be considered that the factors that were a part of the study by The National Agency for Education received increased weight in the prioritization decisions by the municipalities.

116 Berg, interview 2007, claims that a reform of the school system even had to include shutting down the National Swedish Board of Education to make it possible to get it accepted. The National Swedish Board of Education had become a symbol for a badly functioning and micromanaged school system.

117 Carlsson, interview 2007

118 Borg, interview 2007

119 The municipalities' actions can be thought of as having been different if the voucher system had preceded the municipalization. Most likely, their interest in taking over the activities would have been less if they had been exposed to competition.

10. Concluding Discussion

The intent of the municipalization was not in any way to change the contents or activities of the schools, i.e. how teaching should be done or what goals it should have. This, in combination with the fact that, in addition, the follow-up of the activities was strengthened in connection with the municipalization, requires that the causes for the break in the cost development curve – which can be observed – must be sought somewhere other than in any changes in the activities per se.

The economic-psychological factors described earlier can provide such an explanation. From economic-psychological theory, the explanation can be sought in that, among other things, the change of responsible created a possibility of breaking with earlier ideas about how the activities should be handled. Costs most likely ended up on other (mental or real) accounts, which lead to other prioritizations. A cost that was viewed as too small to be a reason for corrective action when it was a part of the National Budget (and in particular if it would have to be handled through a general system of grants where the schools were given grants based on a large number of variables) could be viewed as unreasonably large when it was payable by a specific municipality. In the same manner, it can be assumed that the proximity effect led to a clearer connection between demand for school services and school services offered by the municipality. At the same time, the decision was delayed because politicians at the national level were afraid that a municipalization would bring with it reduced influence and increased differences between different municipalities as regards to the contents of the education.

Effects that are connected to the Prospect Theory may also have played a role. The decision-makers may have overestimated the negative effects of a change and underestimated the positive effects. With the results in hand, it is also possible to see that even those who warned that municipalization could lead to large resource cuts in the domain of schools were wrong. Nor were those who believed that the municipalization would result in a loss of control over the costs proven right. The break in the trend was instead that the curve became more flat and remained more or less at the cost level of the academic year 1990/1991 cost level.

The decision process is interesting in the respect that in spite of the fact that there was a wide-spread consensus about the desirability of a municipalization, it took almost twenty years from when the issue was first raised as an idea, to the time that the final decision was made by Parliament. In this regard, it differs substantially from those standard cases of political decision-making that are described by Kingdon (1995). Nor does the school municipalization fit into the “inertia” model that is described by Borg (2004). In contrast to the cases described by Borg; old age pension, housing subsidies and the ATP-reform,¹²⁰ there was a near consensus regarding the issue of responsible party for the schools.¹²¹ For example, in the case

120 The ATP reform that was decided in 1994 transformed the benefit based pay as you go pension system into a contribution based, partly funded, pension system.

121 On the other hand, there was a consensus about the previous large change in responsible party – transfer of the police force from the municipalities to the national government in 1964, “*A united Parliament was undividedly behind the large reform of the police force*” Persson & Sundelin (1990) p 86

of schools, there was nothing corresponding to the ideologically and rhetorically locked positions that could be seen concerning the pension system, where the Social Democrats opposed changes to the ATP system long after it was clear that the system was not sustainable over the long term under current demographic and economic conditions.

The municipalization of the schools differed from other political issues in that it did not seem to have been driven by any external events or by the media, but constituted an internal political process. This process begun in the first half of the 1970s when initial studies concerning the issue of responsible party were made, and ended when the reform was implemented in 1992/1993. At any one time, there were other issues on the political agenda that were perceived as more urgent. Thus, in spite of the consensus about the necessity of a reform, and in spite of the fact that the Social Democrat Government, that was in power during most period, was of the opinion that the production of social welfare services was a municipal responsibility, the school issue never made it to the top of the pile. It is therefore necessary to do a historical analysis to find an explanation.

In economic terms, the municipalization was rather about reducing the risk for a feared future cost increase than about directly reducing costs. This is also indicated by the fact that the politicians (the national government) were prepared to add more money in an initial stage to induce those who feared that the municipalization would lead to resource cuts, to support the proposal. It can also be assumed that the issue of responsibility was not an issue that would impact large numbers of voters. Certain secondary effects such as changed conditions of employment and salaries for the teachers and changes to the funding of schools can certainly be assumed to have had some impact, but the connection to the change of responsible party is not clear.¹²²

The study of the process, and its outcome, has produced three clear conclusions regarding the economic-psychological effects: (i) There is a clear break in the cost trend in connection with the municipalization. This is according the predictions that are given by the theory. A change of responsible party makes it possible to break up old locked positions and provides an opportunity to re-examine earlier decisions. This means that a change in the cost trend can be expected. Such a break in the trend can indeed be observed in connection with the municipalization. Before the municipalization the costs were increasing in almost all municipalities, but the change in responsible party was followed by almost a decade of stable costs. The possibility cannot be excluded that other effects play a role,

122 If the debate about the uniformity is followed, it can be intuited that there were fears that the students might be impacted negatively by the municipalization. An objection that both the Government and the opposition brought out was that the municipalization might lead to differences between municipalities. This created the risk that some students, at least in relative terms, would receive an education inferior to that given to others. The results in schools during the last 15 years have clearly worsened, but it is difficult to determine if this is because the municipalities are now the responsible party, or because of changes in the education of the teachers, or because of the changes to the curriculums, or because of the new grade system or because of demography. The lowered results are fairly uniform both across the country and comparing municipal and non-governmental schools, and does not appear to have any connection to how much money is spent per student, see further Key Numbers from the National Agency for Education (Skolverkets Nyckeltal) www.skolverket.se

such as institutional changes or changes in value systems in connection with the financial crisis in the 1990s. This is a field for future research. (ii) Economic-psychological effects can be an underlying cause of why the decision took almost 20 years from the time the first studies were presented, in spite of the fact that there was a wide-spread consensus, and most likely a political majority for a change in responsible party for the schools, during the entire period. On the other hand, loss aversion, both among the voters and the elected, and the resulting status quo effects, can explain this development (or lack of development). By overestimating the negative effects of a change and underestimating the positive ones, extra measures became needed to make a change acceptable. Such a measure appeared when Minister of Education Persson could connect the ongoing salary negotiations to the municipalization issue and use the negotiated salary increases to bring the unions on board. Here, timing was of the essence, because the solution was dependent on the municipalization decision and the salary increases being simultaneous. If the decisions had been separated in time, the expected silver lining effect could not have appeared and it would have been much harder to drive the process to a conclusion.

11. References

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Margit Gennser 2007-07-23

Per Borg 2007-02-11

Ingvar Carlsson 2007-09-05

Bengt-Åke Berg 2007-05-20, 2007-10-26

11.4 Data sources

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The "Ädel Reform"

An Economic-psychological Analysis of the Transfer of Government Activities from Counties to Municipalities

Erik Lakomaa

Abstract: In 1992 a large portion of the public elder care in Sweden was transferred from the counties to the municipalities, the so called Ädel Reform. Although there was a wide-spread consensus among politicians about the necessity of the reform, the process took some 30 years. Traditional economic theories might be less suitable for explaining both the slow process and the outcome of the reform. In this paper insights from economic psychology are used as an improvement on more traditional economic theories. This paper covers the political process that preceded the reform, an evaluation of the economic consequences of the reform and an attempt to explain some of the particularities of the reform using economic-psychological theories.

Thanks to Richard Wahlund, Håkan Lindgren, Örjan Sjöberg, Christoffer Rydland, Karin Råde, Marie Johnsson and Hans Sjögren for valuable comments and to Anders Johnsson for help with data. Thanks also to participants at the EHFF seminar at Stockholm School of Economics for comments and suggestions. Financial support from the Jan Wallander Foundation is gratefully acknowledged. All remaining errors are solely mine.

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1. Introduction

On January 1, 1992, the municipalities assumed responsibility for the nursing of the elderly and for parts of the health care of old people, responsibilities previously held by the counties.¹ The municipalities took over the responsibility for 490 hospitals and nursing homes for the sick, totaling 31,000 beds. Additionally, 400 group homes with in all 3,000 residents, 200 day-care centers for people with senile dementia and 130 institutions for outpatient care. Half of the municipalities in Sweden at the same time reached an agreement with the counties about also assuming responsibility for health care in the patient's home.² As a result of the reform, 55,000 people changed employers, from the counties to the municipalities.³ The reform also increased the responsibilities of the municipalities, measured in economic terms, by one fifth⁴

This change of primary responsibility, which was given the name "the *Ädel Reform*" ("*Ädebreformen*")⁵, has been described by the organization "Sweden's Municipalities and Counties" (*Sveriges Kommuner och Landsting, SKL*) as the "largest organizational reform in Swedish history"⁶ This statement can of course be challenged, for example in the context of the move of the schools to municipal administration in 1992, and the re-organization of the Swedish municipalities (and their boundaries) in the 1950s and 1960s, but the quote illustrates how the reform was perceived by those who initiated it.

Despite its wide range, this administrative reform was not a big source of political strife. When the Social Democrat government made a deal with the "Liberal Party" ("*Folkpartiet*") they could have received support from both the "Moderate Party" ("*Moderaterna*") and the "Communist Party" ("*Vänsterpartiet Kommunisterna, VPK*"). The *Ädel Reform* fits into a pattern of change of primary responsibility, which can be said to partly be a result of the ever worsening economy of the public sector and partly be derived from a political doctrine which dictates that the state shall be responsible for securing people's income and that the municipalities shall produce social services. Here, the *Ädel Reform* shows a clear similarity to the transfer of schools to the municipalities which was prepared in parallel, and which

1 Sweden has 21 counties, the concept being a little larger than the Anglophone version; the Swedish county is at least geographically considerably larger than the average US or UK county. The county has primary responsibility for certain things, mainly health care and public mass transit. Each county is divided into municipalities. There are 290 municipalities, each typically with a core city or town, and often a large surrounding area. The surrounding areas are included such that, unlike in the US, there are no "unincorporated areas", every piece of Swedish soil belongs to a municipality and a county. As this paper will explain in detail, the municipality is typically responsible for "social" and "elder" care, schools, and welfare payments, except transfer payments. The municipality is also responsible for the usual municipal issues, such as streets.

2 Jennbert & Molin 2003 pp 39, Socialstyrelsen 1995a p 23

3 The reform was implemented by four new laws, SFS 1990:1402; 1990:1403; 1990:1404 and 1990:1405. Twelve existing laws were changed as a consequence.

4 The net cost to the municipalities in 2002 was 22.2 percent of the total municipal expenditures. Jennbert & Molin 2003 p 47

5 From "The Elder Delegation" ("*ÄldreDElegationen*") – the group which worked on producing the proposal.

6 Sveriges Kommuner och Landsting 2005 p 5

was decided a year before the Ädel Reform.⁷ The intent of this article is partly to describe the process up until the implementation of the Ädel Reform, partly to try to analyze the process from the vantage point of economic-psychological theories. As part of this effort, an attempt is made to explain the idiosyncrasies of the political process, i.e. why the decision was made and what the result was.

Unlike traditional theories, economic psychology allows that people are not strictly rational, and that they, as an example, often employ rules of thumb – heuristics – to arrive at a decision. Empirical studies have shown that these theories have significant explanatory power in many areas, including decisions made in financial markets. The assumption that the same decision models that have shown themselves valid in the financial markets should be applicable on political decision-making is therefore not a very strong assumption. The purpose of this paper is not to try to confirm or falsify the economic-psychological theories; this theory is used as a complement to classic source criticism. To the common criteria one more is added: *”Are the statements in the source material consistent with the predictions given by this theory?”*

Possibly as a consequence of that “issues which concern the county rarely [attract] any interest,”⁸ the Ädel Reform has, despite its large scope, not been the subject of earlier research to any large degree. The closest thing is the evaluation made by Socialstyrelsen (The National Board of Health and Welfare) (Socialstyrelsen 1993, 1995a, 1995b, 1998). Add to that Pierre (1993) and Twaddle (1999), who describe reforms of the public sector in Sweden, but who do not specifically address the Ädel Reform. Nor have there been any earlier attempts to apply economic-psychological theories to political reforms (even if Kingdon, 1995, from a Political Science viewpoint touches on this issue). As we will see, traditional theories like Institutional Theory, Rational Choice Theory or the specialized theories for political decision-making developed by Kingdon (1995) do not get us all the way to explain this process. This paper will therefore, as previously mentioned, use theories from economic psychology as an alternative to the above theories.

This paper will begin with a discussion about the source material used. After that follows a more wide-ranging description of the process that led to the Ädel Reform, and a thorough analysis of the result in economic terms. Finally, the decision process and the result are analyzed through a economic-psychological framework.

7 Even in this case, there was actually a political consensus about the desirability of moving the primary responsibility (Lakomaa 2008). The same was true about the earlier major change in responsibility, moving the police force to the national budget, 1964. *”A united Parliament was undividedly behind the great police reform”* Persson & Sundelin (1990) p 86.

8 Carlsson, interview 2007.

2. Source Material

The presentation in this paper is based partly on official publications in the form of state-sponsored studies, propositions (bills originating from the government), motions (bills originating from Parliament members or groups) and minutes from Parliament, partly on articles in newspapers and professional magazines. As a complement to the printed material, a small number of interviews have been done with some of those who were key persons in some of the described processes.

In several cases, there are additionally the statements of the same person first from Parliament minutes and motions, then from their own memoirs and similar sources, then from interviews. In these cases you cannot exclude the possibility that there is a dependency between the different sources. The presentation is based to only a very limited extent on minutes from Parliament and articles in news media. This is a limitation brought in because the debate of the actual subject matter – the change of primary responsibility – was not done publicly to any great extent, but the proposed reform was used as a pretext for debating various other issues that could somehow be connected to care for the sick and the old, such as questions about resources being made available for this care, private actors in care, issues about availability of choice and general economic issues that concern the elderly.⁹ The motions that were made in connection with the work in Parliament concerning the Ädel Reform often concerned issues about care for the sick and elderly in general, rather than the reform as such.¹⁰

The use of interviews produces the same requirements on source criticism as the use of other source material. It should also be noted, however, that there is a risk that the interviewee is further removed in time than when you go back to for example articles in the press and that there may be occurrences of rationalizations after the fact about decisions that were made.

Because of the nature of the source material, some vigilance is called for regarding biases. However, it is possible to see that, both over time and between the different people, there is a large consensus between the different statements with regard to the overarching events, which makes the problems smaller.¹¹ The interviews have been made to describe the background of the change of primarily

9 It is of course possible to speculate about whether the fear that other care-related questions could appear on the agenda contributed to the fact that the political leadership did not want to make proposals about elder care. However, there is no source material that supports this hypothesis.

10 It is worth noting that one of the motions which was made actually was passed as law, an event that is very rare. The motion was about requirements to institute measures against abuse of the old, and had been made by Daniel Tarschys of the Liberal Party. The motions and Parliament minutes that constitute the source material for this paper are taken from Riksdagen, thus page numbers are missing, as those would vary depending on what search term was used and in which order the material was downloaded

11 The parts of this paper that concern the statements by the then chairman of *Landstingsförbundet* (The Association of Counties), Gunnar Hofring, and the Assistant Minister of Social Affairs Bengt Lindqvist are based to a large extent on the interview which Welat Songur had with Hofring and Lindqvist in 1993. This means that there is a risk that the answers have been filtered, but as they are deceased, there is no possibility of having new interviews with them.

responsible entity, and to complement the written source material. Most of the interviews were made during 2007, the decision about the transfer to the municipalities was made in 1989, i.e. almost twenty years earlier. Concerning questions about the discussions about the limits to the expansion of the public sector, these are events that took place 35 years before the time of the interview. Of course, as time passes, the risk that memories will be incorrect increases, as does the risk that the answer is based on secondary sources. The researcher must allow for this. He should also reflect on the methodology for the interview. In this case, a so-called semi-open interview has been used, this means that initially the interviewer posed open questions, and then the interviewer asked specific follow-up questions, which were however connected to a form with a list of questions. With semi-open interviews (just as with open interviews) there is a certain risk for bias, which the researcher must consider.

2.1 Persons Interviewed

The choice of people to be interviewed was based on the desire to complement printed source material with comments from some of those who participated in the process, as makers of decisions, as advisors, or as listeners. Persons interviewed were Ingvar Carlsson, Lars-Eric Ericsson, Margit Gennser, Per Borg, Bengt-Åke Berg, Sture Korpi and Carl-Johan Åberg. Carlsson was a Social Democrat Prime Minister 1986-1991, i.e. during the time the decisions were made; also he was Minister of Education 1969-1973, which corresponds to the time when the transfer of the schools was finalized as a state responsibility, but also when a move back to municipal control was first discussed and studied. Lars-Eric Ericsson is a Social Democrat and he was the chairman of the Association of Swedish Municipalities (*Kommunförbundet*), 1986-1992. Prior to that, he was a city council member in the city of Uppsala (1976-1986), and he was under-secretary of state in the Ministry of Culture (1974-1976), Margit Gennser was a Member of Parliament for the Moderate Party (Conservative) between 1982 and 2002 and was, during the eighties, her party's spokesperson for municipal issues. She has a background as a municipal politician in Malmö. Carl-Johan Åberg was under-secretary of state in the Ministry of Finance under Minister of Finance Gunnar Sträng and responsible, in 1971, for *Långtidsutredningen* ("The Long-Term Study", an ongoing planning tool in Sweden). As under-secretary, he was a central actor when issues about efficiency and the determination of primary responsibility first were brought into discussion. Bengt-Åke Berg, a social democrat, was Budget Chief in the Ministry of Finance during the first half of the seventies, under Gunnar Sträng, and as such he had considerable knowledge of the policies of budgeting. Later, he became the supervisor for social issues in the City of Stockholm, and in this role he came to see the process from the municipal point of view. Per Borg, a Social Democrat, was also Under-Secretary of State – although in a ministry not affected, the Ministry of Defense – during the period when the decisions about the great changes in primary responsibility in the public sector were made. He has however written extensively on public sector reforms. Sture Korpi is a Social Democrat and was Under-Secretary of State in the Ministry of Social Affairs 1982-1991 and thus the senior official

during a most important part of the process. He was also the Chairman of the *Äldreberedningen* (the preparatory study group) 1982-1987, albeit not a member of *Äldredelegationen*.

The main actors with regard to the shaping of the Ädel Reform were the Minister of Social Affairs, Bengt Lindqvist; the chairman of the Association of Swedish Municipalities (*Kommunförbundet*), Lars-Eric Ericsson and the chairman of the Association of Swedish Counties (*Landstingsförbundet*), Gunnar Hofring. Thus, Ericsson is a very central source. As he is the only main actor that has been available for an interview, there is a risk that the description becomes one-sided. This has been avoided to the largest extent possible by verifying his statements by comparing them with other sources, both oral and printed. As the source material shows great consistency, this is less complicated than one might expect. However, of course there is a risk of collective forgetfulness or bias, which can stem from rationalization of one's actions after the fact, or is based on the presentation being built from sources that the interviewees have in common. Several of the interviewees have also written memoirs or similar material, and these can be used as source material. Few of these, however, describe the Ädel Reform, this applies to Åberg (2006) and Carlsson (2003), which do not mention neither the Ädel Reform nor the Minister of Social Affairs, Lindqvist. Three of the interviewees (Gennser 1982, Åberg 1997, Borg 2004, Borg 2006) have in other contexts written about how one can – or should – reform the public sector, but among these, only Gennser brings up elder care. In her case, it is however mainly a discussion of how travel service (“Cab Vouchers” and the like) have been organized in various municipalities.

There are several other interesting descriptions of the period studied, from participants that were in the Cabinet, for example Feldt (1991), Leijon (1991), Andersson (1993), Sahlin (1996), Hellström (1999), Peterson (1999) and Persson (2007), but they do not mention the Ädel Reform. Maybe this is telling us something about how little weight this issue was considered to have at the level of the national Government, or, in any case, how this issue was deemed to generate little controversy. If the issue had been the object of political conflicts it is easy to expect that the participants (after the fact) would have given differing descriptions of the reality of this reform in order to defend their own acts. The same is true if the reform had failed. Then, there would have been room for presenting the own acts in terms of “*I told you so*”, at least from the opposition, or from people who for any reason felt themselves offended. However, no support for this line of argument has been found.

As the Ädel Reform only to a very limited extent touched on labor market issues, and no labor-union officers had any central positions among the decision makers, no interviews with the labor market parties have been made.

3. The Transfer of Elder-Care to the Municipalities – a historical overview.

The separation of care into care for the sick and care in terms of general welfare has a long history. The first Swedish regulation which separated care for the poor and care for the sick came as early as 1605.¹² According to this regulation, the sick should be tended at a hospital, and the poor would be helped in the parish hall. This was confirmed by Queen Kristina who decided, in 1642, that the sick should be tended at a hospital. The hospitals were regulated by Church Law.¹³ This system remained until the middle of the nineteenth century. The “Poor Law” of 1847 determined that the parishes had the duty to support those who lived in the parish, and that the parishes no longer could prevent people from moving into the parish. Earlier, forbidding people unable to support themselves to move into the parish was a way to keep the cost for care of the poor down.

At the end of the nineteenth century, so-called “*Poor Farms*” (*fattiggårdar*) were introduced. They were a form of municipal Elder Care that combined residency with agricultural work. Typically, these comprised a few hundred people, but there were also some larger units.¹⁴ The Poor Law of 1918 again specified the division between those that were sick and those that needed welfare, and for the first time mentioned government-provided facilities for the aged (“*Ålderdomshem*”). In the care of the needy, the distinction was made between different modes of care. People in need of care should be separated from each other depending on what form of care they required. The municipalities and the counties were given the responsibility for Elder Care, care for the chronically disabled, and long-term care for the sick, while the national government was made responsible for the type of care that is given in larger institutions.

In 1948, provisions of a limited form of home care intended for families with children was initiated, and during the 1950s this inspired the so-called “live at home” ideology, where old people through help and care were assumed to be able to remain in their homes. One of the proponents of this model was the then Minister of Social Affairs Gunnar Sträng, was a proponent of care in the home, not in institutions. This viewpoint was dominant in the Elder Care study of 1952 (SOU 1956:1) which resulted in the 1957 Guidelines for Elder Care. (*Riktlinjer för åldringsvård*) At the same time, the care for the acutely sick and long-term ill among the old was expanded. A requirement was introduced to increase the standard of care at the government-provided facilities for the aged (“*Ålderdomshem*”). The standard in those facilities had been allowed to fall behind those of the rest of society. During the same period, the municipalities took over the in-home help that volunteer organizations such as the Red Cross offered to the old and the sick, but the municipal activity was rather limited. During the 1950s there were about 5,000 “Home Samaritans” (*hemsamariter*) and about one percent of the old had in-home help.¹⁵

12 Socialstyrelsen 1995a p 7 See also Johansson 1991

13 There was no separation of church and state.

14 See e.g. SOU 1987:21

15 Socialstyrelsen 1995a p 5

The issue of who would have primary responsibility – at least since the Elder Care Study of 1952 – goes is central in the debate about elder care. According to the 1968 social study, it is the scope, the time and the place for the care that should determine whether the care should be provided by the municipality or the county¹⁶.

The distinction is difficult to make and the principle that was applied was that the responsibility was dependent on the cause; if the issue was old age in general, it was a municipal responsibility, of the care was required due to illness it was the responsibility of the county.

The study from 1957 was followed by a new study in 1963 where it was proposed that the open modes of care should be expanded.¹⁷ In a later government study, Pensionärsundersökningen (SOU 1977:98), it was proposed that the municipalities should receive money from the national government to provide in-home care, and to improve and modernize the homes of the elderly so that they would be suited for in-home nursing. Also, government loans were to be given out to improve long-term care for the sick.

16 Socialstyrelsen 1995a p 9, Spri s103 1978, Spri s105 1978,

17 SOU 1963:47

4. The Expansion of the Municipal Sector

The largest expansion of both total and the public consumption took place during the early 1970s, which is also the period during which the costs for elder care had its most rapid increase.¹⁸ The biggest expansion took place in 1976, when public consumption increased by almost 17 percent in nominal terms, or about 7 percent in real terms, i.e. after allowing for inflation. The same year, the difference between growth in the public and the private sector was the largest (see diagram 2). The center-right electoral victory in September of the same year was indeed followed by a slower expansion of public consumption, but as a percentage of GNP of the public sector kept growing until 1980 (see diagram 1). The diagram also shows that the growth in public consumption and in public investments takes place primarily in the counties and municipalities whereas the state (national) consumption is essentially constant as percentage of GNP.¹⁹ As an example, the municipal consumption's part of GNP increased from 8 percent in 1950 to 22 percent in 1980, while state (national) consumption during the same time increased from 8 percent to 12 percent. This happened in spite of the fact that important activities such as the police and the schools during this time period were transferred from the municipalities to the national government.²⁰

18 Consumption is spending with public investments and transfer payments subtracted out

19 That the state (national) part of consumption and investments did not increase despite the new areas of responsibility is likely explained partly by the high rate of economic growth during this period, partly by the introduction of the government pension "ATP" system which created room for public investments.

20 For a description of how the transfer of the police force to the national government was done, see Persson & Sundelin (1991) pp 77. Even in this case it was a long drawn-out process. The first proposal about transfer of police to the state was made in 1921. The issue was discussed when the Police Law of 1925 was drafted. In 1939, the "Police Study" made a new proposal about transfer to the state; this was not implemented. The "Police Study" of 1948 instead brought two proposals, transfer to the state and continued municipal responsibility. In 1957, yet another "Police Study" was commissioned, which later, in 1961, brought forth the proposal about transfer to state which was implemented.

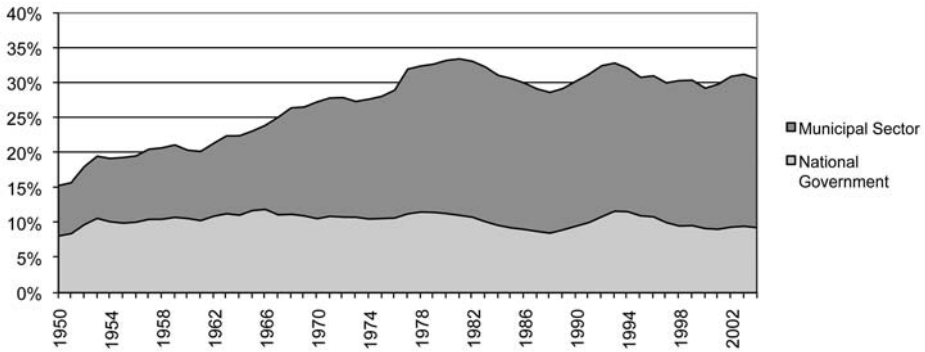


Diagram 1: Public consumption and investments (state vs. county and municipality) as a proportion of GNP 1950-2002 Source: Björklund & Larsson 2005 p 3

Until the middle of the 1970s, both private and public consumption increased very rapidly, and additionally, at an increasing rate (see diagram 2). The diagram also shows that public and private consumption increased rapidly at the end of the 1980s, i.e. just before the decision about the transfer of responsibility to the municipalities. From a falling trend, public consumption turned sharply upward during the years 1987-1988.

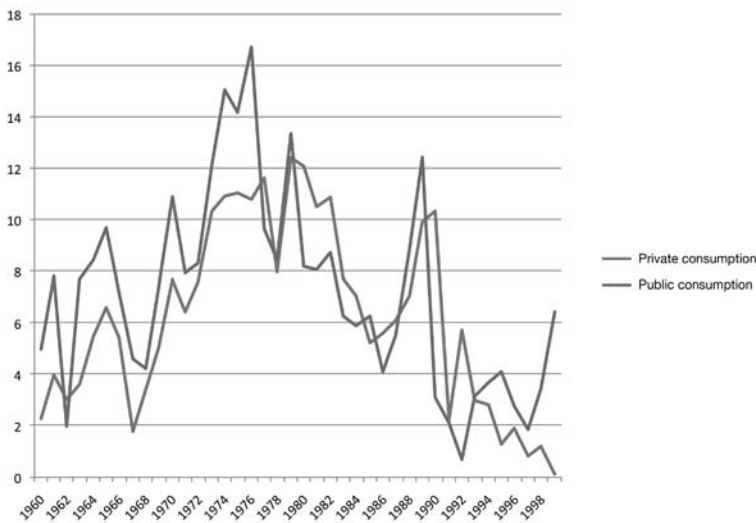


Diagram 2: Private and public consumption 1960-1999, percent change year-to-year. Source: Edwinnson 2005

Public consumption increased, with a few exceptions, faster than private consumption during all of the investigated time period. The exceptions were the years 1962, 1977, 1979-1984, 1989-1993, which can also be seen from Diagram 3.

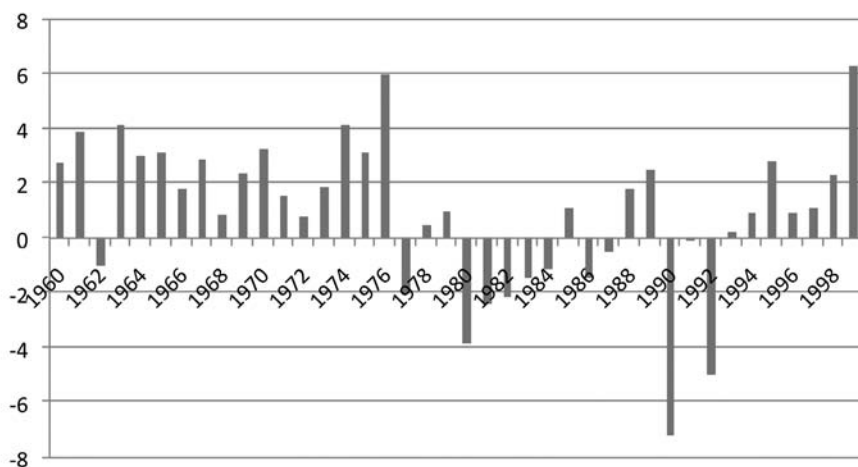


Diagram 3. Percentage change year-over-year for public minus-private consumption 1960-1999. Bars >0 mean that public consumption increased more rapidly than private ditto. Bars <0 mean that private consumption increased faster than public. Source: Edwinsson 2005

The period from the mid-sixties was in general marked by a very large increase in public consumption. In 1965 it was 22 percent of GNP but by 1980 it had increased to 34 percent.²¹ The expansion of Elder Care followed this pattern too. In 1965 145,000 elderly and handicapped people received assistance in the home, six years later that number had more than doubled to 300,000 and by 1975 320,000 people received such assistance. Yet another year later, by 1976, an additional 21,000 recipients of in-home service had been added. The development was similar as regards to other forms of Elder Care. After the action program of 1964 there were 120,000 homes which were improved and during the period 1970-75 there were also 15,000 beds in nursing homes added.²² This was done at the same time that there was an expansion in travel service, food- and bath service, foot care and hobby activities.

During the ten-year period 1965-75, as can be seen from Diagram 4, the number of employees increased in municipal elder care from 20,075 to 82,587 people, that is by more than 300 percent. The increase prior to that was in itself very substantial, but it started from a lower level; during the 1950s in-home services had about 5,000 employees and about one percent of the elderly received in-home care.²³ The services provided by the counties did also increase substantially during this period.

Notwithstanding the substantial expansion, elder care had by no means the same political stature as for example Child Care. Child Care was a central issue in

21 Björklund & Larsson 2005 p 3

22 Socialstyrelsen 1995a p 8

23 Socialstyrelsen 1995a p 7f, see also SOU 1977:98

national politics despite the fact that it is administered by the municipalities.²⁴ For example, the expansion of Child Care was an item highlighted in communications from the Social Democrat government in spite of the fact that it was a municipal issue and the municipalities were strongly pressured to deliver Child Care services.²⁵

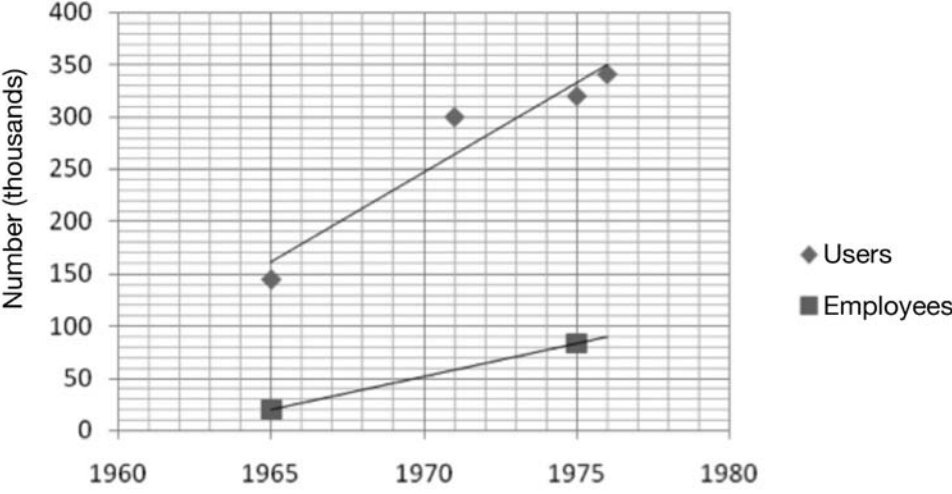


Diagram 4. The number of users and employees within municipal elder care 1965-1976. Source: Johansson (1991), SOU 1977:98, Spri S103 1978, Socialstyrelsen 1995a

24 Interview Carlsson 200, Interview Berg 2007
25 Interview Berg 2007

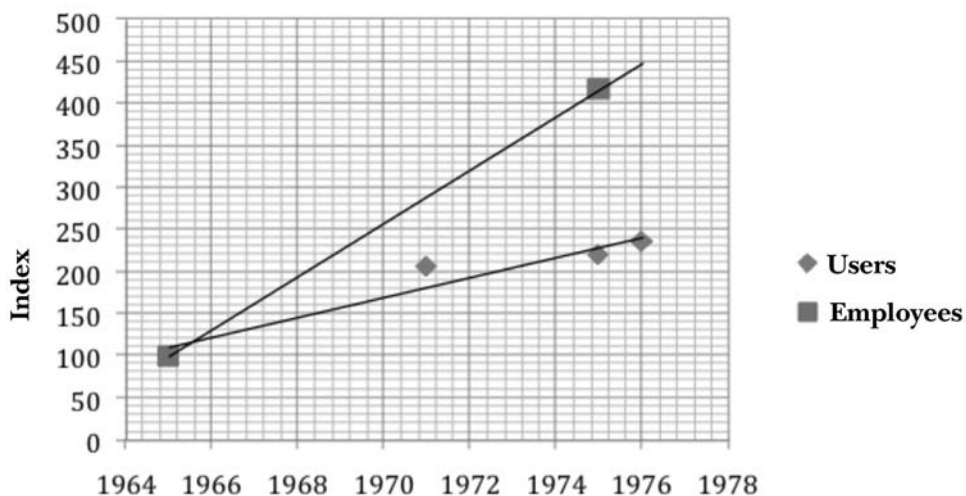


Diagram 5. Percentage change of the number of users and the number of employees of the municipal Elder Care 1965-1976. Index 1965=100. Source: Johansson (1991), SOU 1977:98, Spri S103 1978, Socialstyrelsen 1995a

During the thirty-year period 1974-2004 the total cost for Elder Care increased very substantially. The cost, expressed in 2004 prices, increased by close to 250 percent. A clear change took place in connection with the decision to transfer the primary responsible party. The last year with county responsibility, 1991, was the end of an eighteen-year period of rising costs. During the period after the reform, there are both years with decreasing and years with increasing costs. After the reform, the trend towards increasing costs abated. If you study the period before the Ädel Reform you will find that the costs for Elder Care increased in an even pace during the whole period, corresponding to an increase of 50 percent per ten-year period. Before the Ädel Reform, there was only one year when the costs did not increase, and that was the year immediately prior to the reform, i.e. the year after the decision was made. The number of people over 65 increased during the same period by about 25 percent, which means that the costs per retired person also increased, if not as substantially. During the first part of this period, the increased cost can be explained by that a larger number of retirees gained access to elder care, while the later part of the period, 1984-1991, shows the opposite development. The number of users decreased during these years, at the same time that the costs per user increased substantially. At the time of the Ädel Reform, there were even fewer people who received elder care compared to 1974 (see Diagram 6), this at the same time that the older part of the population had increased by a quarter. The cost per user increased during the period 1974-1992 by close to 240 percent.²⁶

²⁶ Johansson 2005 p 9

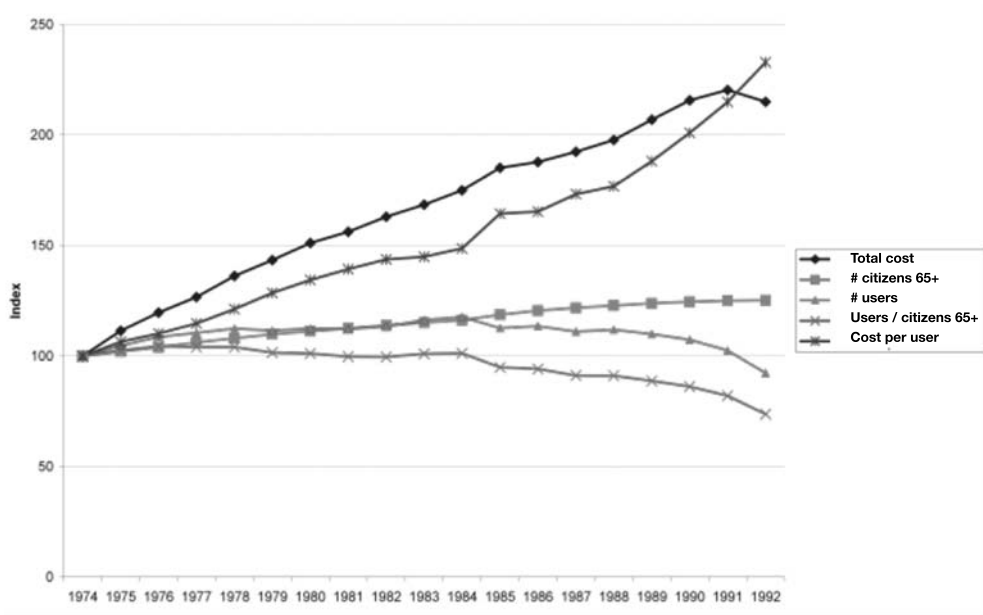


Diagram 6. Comparison between cost changes, (2004 prices) and the changes in population, care recipients etc 1974-1992. Index 1974=100. Source: Johansson 2005 p 9

5. The First Steps toward Transfer of Responsibility – The Elder Committee 1979-1987

Even during the 1970s there were opinions concerning that the organization at the time was not optimal, and by 1976 the Associations of Counties and Municipalities, Socialstyrelsen and ”Sjukvårdens och Socialvårdens planerings- och rationaliseringsinstitut” (The Planning and Rationalization Board for Health Care and Welfare, SPRI, referred to throughout this paper) decided to undertake a joint pre-study of different experimental activities between municipalities and counties and to analyze the problems experienced with the elder care.²⁷ The assumption was that increased cooperation would result in improved care and welfare, and would lead to a reduction of duplicate effort. Socialstyrelsen recommended in conjunction with this study, that the actors concerned should try to find expanded possibilities to make the base for Elder Care their normal place of residence i.e. trying to keep the elderly in their homes.²⁸

In the Ministry of Finance discussions had started during the 1970s about different methods of making the public sector more efficient. At this time, however, no discussion took place regarding the suitability of different responsible parties. Even if a certain risk was seen that the expenditure for the municipalities would increase too rapidly, the connection to the issue of who should carry the primary responsibility was not made.²⁹ As early as during the 1950s the first statements were heard about it being a desired goal to make the municipalities the primary responsible parties for elder care.³⁰ It is, however, not unreasonable to assume that the substantial increase in costs for the public activities was one of the reasons why the discussions about transfer of primary responsibility were accelerated. When problems no longer can be solved by adding more resources, it is quite simply necessary to try to find new organizational solutions.

The development towards transfer to municipal control was expressed during the 1970s by the so called principle of competency. This meant that the municipalities were to supply care-takers and the counties were to supply medically educated personnel.³¹ According to this principle, the nursing homes became a county responsibility and the municipalities were tasked with ålderdomshem service homes and in-home care.

New legislation would also influence the division of responsibilities. When the new Social Service Law (1980:620) became effective 1982, and at that time replaced the Child-care Law, the Sobriety Law and the Law of Social Assistance, this came to mean that the responsibility of the municipalities for the welfare of the residents of the respective municipalities was substantially increased. ”*The Social Service Law gave the municipalities the ultimate responsibility to support, help and aid the*

27 Spri s. 43 1977. A corresponding evaluation was made by Socialstyrelsen after the Ädel Reform.

28 See e.g. Socialstyrelsen 1993

29 Interview Berg 2007, Interview Åberg 2007

30 Socialstyrelsen 1995a p 11, see also Socialstyrelsen 1995b

31 Socialstyrelsen 1995a p 9, se also Spri s103 1978

residents of the municipality”, so writes *Socialstyrelsen*.³² Through the new Health- and Health-care Law (1982:736) the municipalities came to have a more comprehensive responsibility for social services. In the new law, the abovementioned principle of competency became the guide.

Primary health care and Elder Care were at the same time expanded on a large scale starting at the end of the 1960s. The home health care facilities run by the counties were originally to compensate for the shortage of long-time care beds, and up until the 1980s the counties compensated the municipalities financially for the long-term sick that were living in *älderdomsheim*.³³ The new distribution of responsibilities, however, received criticism from both the Swedish National Audit Office (*Riksrevisionsverket*) and from several municipalities and county boards of supervisors. The critics were of the opinion that the division of responsibilities was unclear and that were severe problems drawing the dividing lines. This was expressed in various different ways. In its evaluation, *Socialstyrelsen* writes:

In thousands of groups planning care, the practical division of labor was discussed; for example, could the county vocational nurse cook oatmeal when she was at the care recipients home anyway? Who could give eye drops? And what was the difference anyway between health care tasks and ”tasks of a health care nature”? [...] [The critics] held the opinion that when the resources of the responsible organization become scarce, they will rely on each other’s work.³⁴

This criticism was countered by the center-right government with a claim that a sharper division of labor would ”lead to increased costs, reduced exchange of information [and] would make it harder to [utilize] gains from rationalizations and to utilize spare capacity”.³⁵ The Social Democrat opposition adapted this criticism and demanded that the elder care should be further studied.³⁶ The government took this ad notam, and in 1979 instituted a preparatory study group – *Äldreberedningen* – consisting of the Minister of Social Affairs and the undersecretaries in the Prime Minister’s Office, and the undersecretaries in the Ministry of Social Affairs, the Ministry of Budget, the Ministry of Education, the Ministry of Housing, the Ministry of Labor, and by representatives for the Association of Swedish Municipalities, the Association of Swedish Counties and finally representatives for the retiree organizations *Pensionärernas Riksorganisation* (PRO) and *Sveriges Folkpensionärers Riksförbund* (SFRF).³⁷

After a decision by Parliament 1981 (S 1981:1) the preparatory study was chaired by the Member of Parliament Christina Rogenstam (Center Party), and additionally was staffed by Henry Fager from the Swedish Association of Municipalities, Ingemar Konradsson (Social Democrats), Mårten Werner (Moderate Party) and Eva Winther (Liberal Party). Additionally, a number of experts were associated with the group. After the election 1982 when the Social Democrats formed a government, the chairmanship was taken over by Sture Korpi, undersecretary in the

32 Socialstyrelsen 1995a p 9

33 See e.g. Johansson 1991

34 Jennbert & Molin 2003 p 38

35 Proposition 1979:80:1

36 Motion 1978/79:515

37 These are roughly equivalent to such entities as the US AARP, the American Association of Retired People

Ministry of Social Affairs, and Rogenstam (and thus the Center Party) left the group. In 1984 the Center Party came back to the group, represented by Stina Anderson. At the same time, Karin Nordlander (Communist Party³⁸) was added and Blenda Littmarck (Moderate Party) replaced the Moderate Party member Mårten Werner. The group then kept the same people until it delivered its final memorandum in 1987.

The chairman of the group, the Social Democrat Under-secretary of State in the Ministry of Social Affairs, Sture Korpi, was of the opinion that what was a defining characteristic of the study group was the low political level of its members. "They had no important positions in their respective parties. That includes the Social Democrats."³⁹ However, he at the same time described the group as constituted during the center-right government as "toothless". As regards the group he came to chair, Korpi was probably right as regards to the Social Democrats, the Liberal Party and the Moderate Party. For example both Bo Könberg (Liberal Party) and Margit Gennser (Moderate Party) must be considered as more of political heavyweights in this matter than Littmarck and Winther. The Center Party, however, was represented at a high level, through Rogenstam, until Korpi took over.

The task for the study group was to develop an action program for service, care and welfare for the elderly. The principle of competency was supposed to be guiding. The work was done between 1980 and 1987. The study group resulted in three government study papers about the future organization of elder care: "*Leva som äldre*" (SOU 1985:3), "*Dagens äldre*" (SOU 1985:31) and "*Äldreomsorg i utveckling*" (SOU 1987:21). In the study group's publications, it was pointed out that the then current distribution of responsibilities, or rather, division of responsibilities, between municipalities and counties was such that the elderly could be forced into institutions instead of staying in their homes if county care was expanded but municipal elder care was not. It was also highlighted that the then current organization even in other respects was far from optimal. The problem was also described as that there were two primary responsible parties, with different areas of responsibility, but with overlapping activities with similar content, and additionally groups of employees that were interchangeable. This led to different results for different elderly people needing care.

Here there were examples of older people who by chance either ended up in an *älderdomshem* after an acute illness or at one of the county nursing homes – establishments with very different housing standards, rules for fees and culture of care. It was also possible to be left at the hospital for acute care if the municipality regarded the patient as too 'sick' to live in municipally provided facilities and the county considered the patient to 'well' to be placed in long-term care for the sick.⁴⁰

38 Now "The Left Party" (*Vänsterpartiet*)

39 Korpi, interview 2008. Korpi also claims that Blenda Littmarck became "*very irritated by my arrival and my way to lead the work, and accused me of having caused various diseases from which she suffered*". Korpi must not remember this right as Littmarck joined the group not until two years after Korpi had become chairman, but clearly, the spirit of cooperation in the group was not of the best.

40 Socialstyrelsen 1995a p 12

The tools available to the government to direct elder care during this period were primarily different types of state subsidies, and the ability of the state to influence the direction of municipal elder care by using different types of directed payments can be said to have been of large scope. The rules for state contributions in 1983 gave payments to the municipalities for aides in the at-home service with the intent to make the municipalities work on keeping the elderly in their private homes. In addition, a general yearly contribution was given by the state of between 250 and 350 SEK – Swedish kronor (about USD 35 to 50) per municipal resident with old-age or disability pension. The result was that the incentive for the municipalities to continue to operate *ålderdomshem* was reduced as there were no state subsidies for these. Many *ålderdomshem* were in fact taken out of commission. Instead, efforts were made to use different forms of "assisted living" (*serviceboende*), i.e. homelike settings with staff available to help as necessary. In 1989 the rules were changed for the state subsidy, so that the municipalities instead received 34,000 kronor per year for each employee with "care" tasks, and 17,000 kronor per year for each person in a full-time care facility. These rules had the result that the municipalities to some extent returned to running *ålderdomshem*.

Even the preparatory study group held the opinion that parts of the problem within elder care could be solved by increasing the state subsidies, e.g. the transfer of responsibility for elder care in institutions would be easier if the municipalities could at the same time expand in-home care and increase the number of employees in the assisted living facilities.⁴¹ Several of the problems which the preparatory study group analyzed indicated the difficulties with two primary responsible parties and the problems of drawing the boundary lines became an important area of study for the group. Additionally, the issue of primary responsibility could easily become more emphasized as the costs for elder care increased, which was expected as the number of elder people was increasing.⁴² Incorrect allocations were many times described as resulting from lack of resources. Two out of five patients in long-term care for the sick could, if their need for care was the concern, have been able to live in their homes, but the shortage of in-home service and suitable living quarters prevented them from being discharged from long-term care facilities.

The preparatory study group finished its work in 1987, but did not produce any proposals as to how the problems should be solved. But the group made clear the difficulty with two responsible parties. This conclusion resulted in a proposition from the Social Democrat government. This was probably made easier by the fact that both the Minister for Social Affairs, Lindqvist, and the chairman of the Association of Swedish Counties, Ericsson, had expressed criticism similar to that coming from the preparatory study group. They were of the opinion that the principle of competency created structural problems; that the counties and municipal social services had parallel organizations, for example the in-home health care, and the in-home social services were overlapping. There was, ac-

41 Socialstyrelsen 1995a p 12, see also Songur 1993, SOU 1985:3

42 The cost per user increased substantially during the whole of this time period up to the Ädel Reform 1992, while the proportion of the population above 65 years of age was fairly stable from 1974 to 1984 and decreased after that. Johansson 2005 p 9

ording to them, a risk that a person could be classified as too sick to stay at home but too healthy to be in a hospital.⁴³

6. The Elder Delegation 1988-1989

The abovementioned proposition (bill) did not suggest that the municipalities should take over the responsibility for elder care; however it included writings that opened up for further discussion, i.e it said that a reform was necessary.⁴⁴ The Assistant Minister for Social Affairs Bengt Lindqvist took the proposition as starting point and begun to assemble support within the party for a reform.

In April 1998 Lindqvist, Carlsson, Ericsson and Hofring met and tried to agree on a common Social Democratic policy regarding the responsibility of the Elder Care. Their meetings did not result in a consensus agreement (the Party line was to be Ericsson's and Lindqvist's) but they decided that a delegation should be formed in order to discuss the issue.⁴⁵ The delegation – The Elder Delegation (*Äldredelegationen*) – started its work in October of 1988 and finished in May of 1989.

The Elder Delegation's tasks were (i) to analyze the consequences of a change in primary responsibility, (ii) to discuss which changes would be required within the municipalities and the counties as a result of the change in primary responsibility, and (iii) to study the economic issues such as state contributions and the reorganization of the tax structure. At the beginning, the delegation was composed of Social Democrats exclusively; Assistant Minister of Social Affairs Bengt Lindqvist, the chairman of the Association of Swedish Counties Gunnar Hofring and the chairman of the Association of Swedish Municipalities Lars-Eric Ericsson.⁴⁶ The delegation was to negotiate a solution based on the guideline from the Social Democratic Party Board, and Prime Minister Ingvar Carlsson was of the opinion that it was time to stop bickering and decide on something.⁴⁷ From the center-right opposition there were objections to the fact that the delegation was a purely Social Democrat construct, to which Lindqvist replied that a small group “*could work more easily*.”⁴⁸ However, the government ended up enlarging the delegation by adding representatives from the opposition: Anita Estberger (Moderates) who was on the County Board of Supervisors in Kopparberg County, Bo Könberg (Liberals), on the County Board of Supervisors in Stockholm County, and Ingrid Zetterström (Center Party) who was the Vice Chairperson in the Association of Swedish Counties. Songur writes:

A delegation of nothing but Social Democrats would risk that the reform of Elder Care would be seen as a purely Social Democratic proposition which would make it difficult for the government to get their proposals passed by Parliament.⁴⁹

43 Ericsson interview 2007

44 Songur 1993 p 3, Prop 1987/88:176

45 Songur 1993 p 4

46 Songur 1993 p 4

47 Songur 1993 p 4

48 Songur 1993 p 4

49 Songur 1993 p 4

Lindqvist was of the opinion that the best thing would be to transfer all of elder care to the municipalities. Ericsson agreed in principle, but suggested that "all of primary care plus parts of long-term care for the sick" should be transferred to the municipalities.⁵⁰ According to Ericsson, this suggestion was received "with sympathy" from Lindqvist.⁵¹ Thus there was, he assumed, even before negotiations had started, support for the transfer of elder care to the municipalities, and maybe a possibility to transfer to the municipalities additional county care activities.

Even if there was no externally observable outspoken support for the approach of the Association of Swedish Municipalities, it was in any case clear that the new Elder Delegation had received a clear mandate to negotiate the issues of primary responsible parties. Within this delegation, however, as we shall see, there was a clear conflict between those who spoke for the interests of the counties and those who spoke for the municipalities. The intent was that the delegation would try to bridge these contentions.

If Lindqvist and Ericsson were approving of the reform, this was not true of the third Social Democrat in the group, Hofring. Nor did he subscribe to the definition of the problem. "Actually, the whole thing is a Stockholm problem and to solve it you don't need to change the whole system."⁵² If a transfer of primary responsibility were to be made, the counties could take over all the responsibility for Elder Care, as the competency for health care was already there, he said.⁵³ Further, Hofring believed that the problems were caused by a collision between the culture of social services and the culture of medicine.⁵⁴ "In Malmö and Gothenburg, they had the same problems in spite of the fact that the municipalities had the primary responsibility for both medical care and social services."⁵⁵ Gennser, who had experience of municipal politics in Malmö, like the chairman of the Association of Swedish Municipalities, Ericsson, were of a different opinion. They claimed that the problems in Malmö and Gothenburg were caused by the fact that despite the municipal primary responsibility, the work was organized like a "mini-county" within the municipality. Nor could the problems in Malmö and Gothenburg be said to be worse than elsewhere.⁵⁶

Berg describes the issue as a struggle between the Association of Counties and the Association of Municipalities, which was partly due to the fact that the Association of Municipalities had increased in relative importance.⁵⁷ It was thus difficult for the representatives from the Association of Counties to agree to something that was advocated by the Association of Municipalities. "Above all, the Association of Municipalities and the Association of Counties appeared as two antagonistic entities."⁵⁸ Gennser claimed that there was no deep dividing line between the center-right

50 Ericsson, Interview 2007

51 Ericsson, Interview 2007

52 Hofring, interview in Songur 1993

53 Hofring, interview in Songur 1993

54 Songur 1993 p 5

55 Hofring, interview in Songur 1993

56 Gennser interview 2007, Ericsson interview 2007. Both Gennser and Ericsson are, however, of the opinion that it was correct that representatives of the Association of Counties used to utilize this argument

57 Berg interview 2007

58 Johansson, 1993, the same impression is given by Berg interview 2007 and by Ericsson interview 2007

opposition and the government regarding the substantive issues, and Ericsson agreed.⁵⁹ Before the decision was made, it might look like a conflict based on party politics. This is, however, not quite correct, they both maintained.

The dividing line, according to Gennser and Ericsson was instead to be found between those who represented the interests of the counties and those who represented the interests of the municipalities in the Elder Delegation, and between the Association of Municipalities and the Association of Counties. However, these dividing lines coincided with the party lines, as the municipal interests in the delegation were represented by Social Democrats. According to Ericsson, this was a coincidence that the delegation came to have that very composition and he further held the opinion that it was easier to reach an agreement with the county politician Bo Könberg (Liberals) than with county politicians from his own party.⁶⁰ Korpi, on the other hand, brings out the question of ålderdomshem as a question with party-political conflict, and refers to the fact that the Moderates used this issue in the election campaign 1985.⁶¹

In the delegation, there was a majority on the side of the Association of Municipalities and Ericsson, and it had been possible to disregard the interests of the counties. This had, however, led to a conflict within the Social Democrats, and absent the support from Hofring, the reform could have damaged the government in the election campaign coming up. For some time, it looked like the whole change would not happen. The government was wrestling with internal problems, and there was a government crisis in 1990. The Communist Party voted with the center-right opposition in a vote of no confidence against the Social Democrat government. At the same time, the Liberal Party was pushing the issues of care very strongly, and an internal conflict between Hofring and Lindqvist or (or between Hofring and Ericsson) could thus have damaged the government.⁶² Korpi was of the opinion that there were “*severe conflicts*” within the Social Democratic Party concerning the questions of simple health care at Ålderdomshem and that there were meetings where both the Prime Minister and the Minister of Finance cooperated in the “*intent to bridge interests*” regarding this issue.⁶³

One of the reasons for the threatened collapse could be that the counties – or at least the chairman of the Association of Counties Hofring – misjudged their negotiating strength and hoped to be able to divide the representatives for the municipalities. Bengt Lindqvist claimed that the municipalities were well aware as to how strong their position regarding the substantive issues was, at the same time that the counties were not.⁶⁴ The Counties had difficulties seeing that a transfer of primary responsibility should make any positive contribution whatsoever. One explanation for this is that the issue had been conflated with the question of the future of the counties.⁶⁵

59 Gennser interview 2007, Ericsson interview 2007

60 Ericsson, interview 2007

61 Korpi Interview 2008

62 Sungur 1993 p 2

63 Korpi, interview 2008

64 Ericsson interview 2007

65 See e.g. Socialstyrelsen 1995a pp 24-28. Socialstyrelsen 1995b pp 16-18

The opposition from Hofring resulted in that an agreement between Lindqvist, Ericsson and Hofring was not possible, and to force the issue through, Lindqvist found himself needing to go to the Prime Minister for support. As the Prime Minister strongly backed Lindqvist, the room for negotiations for Hofring (and later the center-right county representatives) was reduced, as a compromise demanded that the Social Democratic Party Board changed its opinion. Bengt Lindqvist had continuous support from Ingvar Carlsson, and he had already, at an earlier time, given Lindqvist the responsibility for Elder Care, in spite of the fact that Gertrud Sigurdsson, as Minister of Social Affairs, was responsible for both health care and social services. Thus, he had a special mandate for the transfer of primary responsibility.⁶⁶

Hofring claims that Lindqvist and Ericsson used the decision of the Party Board as trump to advance their position.⁶⁷ Because of this, Hofring had to yield. "*The alternative would have been to resign as chairman of the Association of Counties. That would have served no purpose, as the Party would have followed its agenda anyway.*"⁶⁸ Hofring's view is precisely that which you would expect from somebody in his position. By referring to the Social Democratic Party his failure to negotiate appears smaller. He did what he could, but against a vastly superior opponent. At the same time, Ericsson indicates that the issue by no means was decided ahead of time.⁶⁹

It is possible to speculate whether the government really wanted a deal spanning the Social Democrats and the opposition. All the representatives for the opposition came from the counties, and it was known that the county politicians were less favorably inclined to the reform than representatives for the municipalities. The Social Democrat representatives were at the same time, with the exception of Hofring, from the municipalities or from Parliament. Margit Gennser is, however, of the opinion, that the reason the Moderates were represented by Anita Estberger, who at the time was on the County Board of Supervisors in Kopparberg County, was a foxes-and-hounds game between those who wanted to abolish the counties and those who wanted to keep them, and where Estberger became the compromise candidate.⁷⁰

If I don't misremember entirely, this was a horrible game of foxes-and-hounds. Ingegerd [Troedsson] who meant a lot, everything, in the social issues, was very keen on keeping the counties. Göran Lenmarker on the other hand wanted to abolish them. On my part, I believe that what was required was a mixed model. The conditions were so different. The small municipalities were probably not able to handle health care (the Ädel Reform, however, demanded some health care), whereas the

66 Songur 1993, Carlsson Interview 2007. Lindqvist was a government minister so it was not controversial to let him remain. When Palme made him a minister after the electoral victory in 1985, however, this was not done with any thoughts about transfer of responsibility. Sten Andersson, for example, writes in his memoirs that he himself was the person behind making Lindqvist a minister – suggested by his (Andersson's) wife – and that the intent was to get an assistant minister of social affairs who could help Sigurdsson to counter Finance Minister Feldt. He also writes that Ingela Thalén was his first choice. (Andersson 1993 p 366)

67 Songur 1993 p 8

68 Hofring intview in Songur 1993

69 Ericsson interview 2007

70 The abolition of counties was an important issue in the elections 1991, and was one of the main issues raised by Ny Demokrati. The Moderates and the Liberals also pushed this issue to a varying degree.

most of the municipalities in the Southern parts of the country should have been relieved of the counties.⁷¹

Ericsson also emphasized that an agreement involving both government and opposition was wanted, and gives the same view as Gennser regarding the counties. If he had had the power to decide, the counties would have been abolished and he is of the opinion that, rightly, there was a concern among county politicians that that would indeed become the case.⁷² Korpi even thinks that it was the question of whether the counties were to be or not to be which made the Association of Counties so strongly oppose the transfer of responsibilities for Elder Care to the municipalities.

Strongly opposing the whole idea stood the Association of Counties. The explanation is that at the time a debate had flared up concerning the existence of counties. The Moderates were pushing this issue with certain intensity and this of course scared the politicians on the county side.⁷³

When the proposition (government-originated bill) was presented, the Center Party, unlike the rest of the opposition parties, called for a vote against the main guiding ideas. They were of the opinion that the intended goal would not be reached, and that the reform instead would create new problems: "*The proposition is not a reform of Elder Care, it is an organizational rearrangement*", they wrote, and it is "*a reform without regard to people's need for care and welfare. The elderly will not get better care.*" In their motion it is also stated that "*it is the issue of who has primary responsibility that has been put in the foreground, not the needs of the elderly and handicapped for care and service.*" The reform should therefore be seen as "*a result of a study made by a group whose members were appointed from above, and an intense battle between the leadership of the Association of Municipalities and the Association of Counties.*"⁷⁴

The Center Party also objected to the financial risks that they believed followed from the proposition from the government. They also claimed that the municipalities, which had financial problems already, would have a difficult time implementing the proposals: "*To give the municipalities comprehensive responsibility for care and service of elderly and handicapped is to put the municipalities to a very tough test.*"⁷⁵ Further, they claimed that the consequences of the proposal were hard to foresee. "*For an equalization between the municipalities, an extremely complex transfer system*⁷⁶ *is sketched out*"⁷⁷ and expressed the opinion that "*the personnel in health care are worried*"⁷⁸ facing this reform. Gennser (Moderates) agreed to the latter point, and said that the opposition from physicians and nurses had to be considered; they were "*not particularly happy about getting the municipalities as primary responsible parties*"⁷⁹

71 Gennser interview 2007

72 Ericsson interview 2007

73 Korpi, Interview 2008

74 Motion 1990/91:So20, Motion 1990/91:So13

75 Motion 1990/91:So20, Motion 1990/91:So13

76 i.e. transfer of money from richer municipalities to poorer ones

77 Motion 1990/91:So20

78 Motion 1990/91:So20

79 Gennser 2007. The reason was probably the same as that which lay behind the teachers' union's resistance to transfer of schools to the municipalities, specifically that municipal employment could be assumed to be worse in terms of both salary and status than government or county employment.

Other parts of the Center Party's criticisms of the proposal were of a more instrumental nature and was more in accordance with those of the other opposition parties. The Center Party claimed, among other things, that it was wrong to assign so much money to information when there were people waiting in line – figuratively – for care.⁸⁰ In the proposition, it was suggested that a billion kronor [about 150 million USD] should be spent to inform and educate those who worked within Elder Care and health care about the reform. In the final decision, this was reduced to 500 million kronor.⁸¹ The earmarking of money for information created strong criticism. “[It is] hard to believe that the proposals will lead to a more humane and efficient care. Further, in the proposition, a billion kronor is earmarked just for information about the proposal!” wrote the Center Party Members of Parliament Hansson and Jönsson in a motion.⁸²

Further, in the opinion of the Center Party, like the Moderate Party and the Liberal Party, the individual responsibility and the role of relatives should be strengthened, and private care givers should not be impeded. “A change in primary responsibility must not mean just that the county and the municipality finance and produce care and welfare on their own.”⁸³ The Center Party wanted that a reform as large as the Ädel Reform should be preceded by a pilot project, and the County of Kalmar was suggested.

Lindqvist was at the same time completely expecting and wanting that the reform should indeed be done.⁸⁴ He spoke about different “levels of change” where, among other things, one alternative was to completely transfer primary health care, and parts of long-term care to the municipalities, another alternative to transferring just elder care. These alternatives would constitute the ceiling and the floor in the negotiations with Hofring and Ericsson.⁸⁵ Lindqvist had thereby “framed” the decision to be about what extent the change would have, and not about whether some change should happen at all.

By framing the alternatives so that only those proposals that brought change were left, and thereby creating a new reference point, Hofring had, in fact, already lost the negotiation ahead of time. Ericsson is of the opinion that the strategy of presenting change as a given and then discussing its scope was “enormously important for the result”.⁸⁶ If Hofring would have any chance of passing the “county opinion” he would have had to launch a counterproposal, such that all Elder Care would be coordinated under one primary responsible party. Then, it would have been possible to keep the door open for a later discussion about who would shoulder the new responsibility, the municipalities or the counties. In such a decision-making situation, it would have been easier for Hofring to get attention to his arguments about the quality of medical care.

80 The Communist Party was also critical of the spending on information. Motion 1990/91: So18

81 Proposition 1990/91:14

82 Motion 1990/91:So13

83 Motion 1990/91:So9, Motion 1990/91:So10, Motion 1990/91:So11, Motion 1990/91:So12, Motion 1990/91:So12, Motion 1990/91:So17, Motion 1990/91:So19, Motion 1990/91:So20, Motion 1990/91:So22, Motion 1990/91:So23

84 Sungur 1993 p 3

85 Sungur 1993 p 3

86 Ericsson interview 2007

Hofring realized that he was already on the losing side when Ädel began its work.⁸⁷ The way out would have been to align himself with the opposition, but as both the Moderates and the Liberals supported the reform in principle, the room for maneuvering was limited. To be sure, the representative for the Moderate Party, Estberger, was not in favor of change, and additionally, she represented the counties. She was, in Gennser's opinion, at the same time not very good at promoting her ideas.⁸⁸

The in principle favorable opinion of the opposition to the transfer of primary responsibility is reflected in the follow-up motions that were introduced. Throughout, the focus is on details, and on different types of additional proposals to increase the freedom of choice within health- and elder care.⁸⁹ The Moderate, Gennser's, and the Liberal, Godin's and the Center Party Israelsson's common motions are good examples of this. In one motion, they highlight the importance of freedom of choice regarding physicians.

The elderly must get or have rights secured to have continued right to their own choice of physicians, even when the municipality has the main economic responsibility for their living quarters and the care that is associated with that.⁹⁰

In another common motion they call for stimulating measures to induce the employees of the county to start their own businesses, and propose that government support of information about this should be made available.⁹¹

The criticism on principle against the proposal as such came from the Center Party, headed by Olof Johansson.⁹² But even at the Center Party, the most powerful criticism was directed to the manner in which the issue was handled. In one motion, Johansson, inter alia, writes that the Center Party is

[Strongly] critical of the Government's handling of the Elder Care issues. [...] Municipalities and counties have, based on a six-point program from the Social Democratic Party Board, been told to start studies and negotiations about the organization of future Elder Care. This demand has not been preceded by any decision in Parliament. [...] This mode of operation is in conflict with all principles of democracy.⁹³

The Minister of Social Affairs, Lindqvist, was at the same time of the opinion that *"he who does not go to his party when facing a major question, when there is deep dis-sention in the party, that person is not functioning well."*⁹⁴

87 Sungur 1993 p 7, this view is confirmed by Gennser, interview 2007

88 Gennser interview 2007

89 Note that the Elder Delegation highlights freedom of choice as a value to the realization of which the reform should contribute. This can reflect the newer more market-oriented or libertarian currents in society but came back in the Social Democrats' discussions about power over self and consumer influence. For a discussion about this, see Ljunggren (1994)

90 Motion 1990/91:So10

91 Motion 1990/91:So12

92 Motion 1990/91:So20

93 Motion 1990/91:So20

94 Lindqvist, interview in Songur 1993

As the Liberal Party was interested in an agreement and as Lindqvist had a mandate to negotiate with that Party's representative in the delegation, Bo Könberg, it was possible to circumvent the practical criticisms from the Center Party but it limited the government's room to negotiate, as it made it impossible to reach an agreement with the Center Party and thereby the government's negotiating position was weakened.

Bo Könberg was very well aware that without him there would be no reform. I could not reach an agreement with the Moderates, I had no mandate [from the Social Democrats] for that. Könberg knew this."⁹⁵

To reach an agreement in a question like this with the Communists was less attractive; a solution spanning the Social Democrats and the center-right opposition was desired, this to prevent that the reform would be rescinded if the government were to change. Additionally, the Communists were regarded as unreliable.⁹⁶ The result was a deal with the Liberal Party where an extra billion kronor were earmarked to contribute to the Liberal Party's demand for single-occupancy rooms in long-term care.

A proposal was developed and circulated for remit⁹⁷ until November of 1990.⁹⁸ The government then sent a proposition [bill] to Parliament, but there the detailed financial questions had been deferred to a future time.⁹⁹ The decision about a transfer of primary responsibility was made by Parliament on December 13th, 1990, and the reform was implemented as of January 1st, 1992.

95 Lindqvist, interview in Songur 1993

96 Berg interview 2007

97 Swedish: *Remissbehandlades*

98 DS 1989:27, see here also Motion 1990/91:So14, Motion 1990/91:So15, Motion 1990/91:So21

99 Proposition 1990/91:14

7. The Economic Results

During the two decades that preceded the Ädel Reform, the costs for Elder Care increased at an even rate. In 2004 prices, they increased by about 220 percent between 1974 and 1991. The year 1991, which was the last year when the counties still were the primary responsible parties, was the first year when the costs for Elder Care did not increase.

After 1991, the trend was broken. The proportion of elderly increased, which has influenced the cost development. Additionally the methods for dividing Elder Care have changed over time, for example concerning the provision of living quarters. Because of this, "*Sveriges Kommuner och Landsting*" (Sweden's Municipalities and Counties, SKL) has calculated how the costs for Elder Care would have developed if the consumption patterns had been constant.¹⁰⁰ By combining the numbers for how the population has varied in differing age groups with the consumption of Elder Care a certain year, it has been possible to develop a comparison figure for Elder Care.

The years that were used were 1974 and 2004. The numbers are nevertheless not fully comparable, because in 1974 there is age data only for the elderly who were provided with living quarters, but not for those who had in-home service, for example. On the other hand, there are detailed figures for actual consumption within different age groups in 2004.¹⁰¹ For a person aged 80 years or more the costs in fixed prices, according to the 1974 consumption pattern, has increased from 80,000 kronor in 1974 to 127,000 kronor in 2004.¹⁰²

As can be seen from diagram 7 and diagram 8, the changes in the cost development depend almost entirely on that the pattern of consumption has changed.¹⁰³ If the pattern of consumption had been constant, no large changes from the Ädel Reform could have been observed other than that the rate of cost increase has abated marginally.

The actual costs changed both as a consequence of that the cost per recipient changed, but also – and more clearly – as a consequence of that the consumption pattern, i.e. the mix of services that were consumed, changed. The Ädel Reform was followed by a fairly strong cost increase during the period 1993-1995, after which the costs strongly decreased.

100 Johansson 2005 p 9. The "consumption pattern" is the term for the mix of Elder Care and Welfare services, and for the age distribution among the users, as it was any specific year. The consumption pattern 2004, for example, denotes the costs if the mix and the age distribution each year had looked like it did in 2004

101 Johansson 2005 p 8

102 Johansson 2005 p 9

103 A clear result of the Ädel Reform is that a larger part of Elder Care was concentrated to the oldest and sickest retirees.

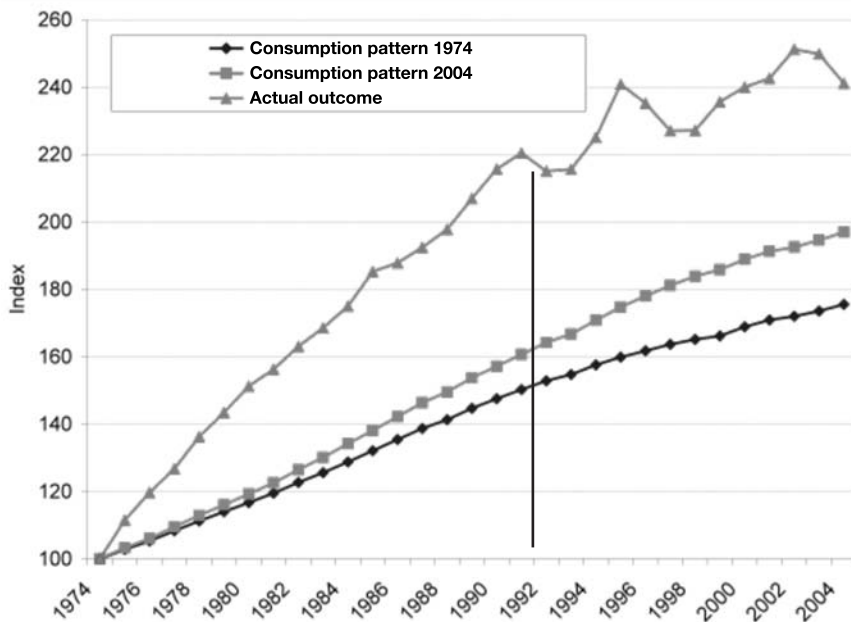


Diagram 7 Comparison between actual cost development (per elderly person) within Elder Care and welfare, and expected cost development if the consumption patterns had been constant, 1974 to 2004. Index for 1974 = 100. Consumption pattern 1974 shows the cost if the mix of elder care and welfare had looked like it did in 1974. Consumption pattern 2004 shows the cost if the mix and age distribution had looked like it did in 2004. Actual is the actual cost development with allowance for that the mix and age distribution changed. Source: Johansson 2005 p 9

The nicks in the curve can have several causes, one is a change in how the costs were calculated. Here, SKL has adjusted the *Ädel Exchange Amount*¹⁰⁴ of 22.3 billion SEK for salary- and price increases between 1991 and 1992, but new costs were added due to the handicap reforms during the 1990s.¹⁰⁵ Further, deferred investments can explain some of the variation.

The transfer of primary responsibility had as a consequence that different types of investments that otherwise would have been made were deferred until the municipalities had taken over and familiarized themselves with the new activities. Changed preconditions because of the general economic development influenced this side of the reform. Facing the *Ädel Reform* it had been calculated that the costs for new buildings, especially in Stockholm, would increase because of the construction boom. This led to municipal demands for compensation. Subsidies were wanted for installations of elevators, government loans for the construction or renovation of elder homes and other forms of elder residences and for preemptive purchases of real estate for elder living.¹⁰⁶

104 Swedish: "*Ädelväxlingsbeloppet*"

105 Johansson 2005 p 9

106 See e.g. Socialstyrelsen, 1995 b. The Swedish municipalities have the right to "preemptive purchases", i.e. when a real estate sale/purchase is concluded, the municipality has the right to pre-empt the buyer and take over the property on the conditions in the contract

An additional problem was the buildings in which the Elder Care had been carried out when the counties were the primary responsible party. They were military-style blocks for which it was not particularly easy to find a new use.¹⁰⁷

Because of the finance- and real estate crisis and the recession, these fears did not fully materialize, but the problem of disposing of older, non-suitable properties, remained.¹⁰⁸

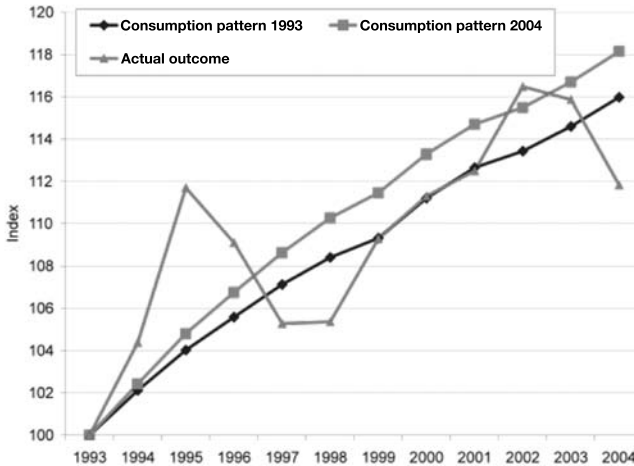


Diagram 8 Comparison between actual cost development (per elder) within elder care and elder welfare and expected cost development if the consumption pattern had been constant, 1993-2004. Index 1993=100 (2004 prices). Consumption pattern 1993 gives the costs if the mix of elder care and welfare services, and the age distribution, had remained the same as it was in 1993, consumption pattern 2004 gives the costs if the mix and age distribution had been the same as it was in 2004. Actual is the actual cost development allowing for that the mix and the age distribution changed over time. Source: Johansson 2005 p 9

With the same consumption pattern as 1974, the costs had increased by 25 billion kronor (corresponding to 75 percent) during the period under study. The actual outcome was an increase of 47 billion kronor, or 141 percent.¹⁰⁹ Even when the 2004 consumption pattern is used as a reference, the costs will be found to have increased by a large amount. This is probably because of the fact that in later years, (after the Ädel Reform), the Elder Care efforts have been concentrated to the oldest groups, more than would have been done if the 1974 consumption pattern

107 Gennser Interview 2007

108 In this paper, no attempt will be made to evaluate the quality of the care and welfare. This is a special area of research and it is not a priori possible to say that any changes that happened are those that are a consequence of the Ädel Reform. Twaddle (1999) p 10, pp 92 and p 116, however, claims that the quality was decidedly decreased but does not describe in what respects, but he refers to Johansson (1993) who writes that there have been a string of articles in the news dailies which have pointed out how the quality has worsened, or to non-verifiable sources and he himself talks about "anecdotal evidence" (p 93). Socialstyrelsen (1993) notes that the quality was a question that demanded attention and SPRI in 1993 worked though the debate in the newspapers about the reform. In those, there is evidence for both positive and negative reactions.

109 Johansson 2005 p 9

had been maintained.¹¹⁰ That the costs increased during the period 1992-1998 can be partially explained by how the care for the handicapped has been calculated in connection with the various reforms in that area. At the same time, there may have been transfers of resources from Elder Care to handicap care or vice versa.

The handicap care that had previously been provided by the counties was transferred to the municipalities during the years 1990 to 1997. In addition to the Ädel Reform, several reforms of handicap care were implemented during the 1990s, such as LSS and LASS 1994 and the psychiatric reform of 1995. This makes it somewhat harder to compare but the Association of Municipalities has compensated for this in its compilation of the cost development. The clearest effect as regards to the cost development is nevertheless that in connection with the Ädel Reform, the curve has a break. The evaluation done by the Association of Municipalities supports the view that the transfer of the principal responsibility has had as a result that the politicians have abandoned old rules for how to run Elder Care and that a larger part of Elder

Care has become concentrated on the very oldest.¹¹¹ The development has partly been driven by the need for the municipalities to prioritize.

The new role of the municipalities as principals for health care is an important explanation for the dynamic development. The total municipal resources have not increased in step with the demographic development and must therefore be used with increasing efficiency.¹¹²

The increase in efficiency can also be a consequence of that the goal that was the purpose of the reform was actually achieved: To avoid duplication of effort and make sure the patients that did not need hospital care were in fact not cared for in hospitals. With the Ädel Reform, a new economic system of controls was introduced: the municipal responsibility to pay.¹¹³ When the physicians at the hospital judged that a patient no longer needed acute hospital care, the municipality was notified that the patient's medical care was completed. If the municipality could not then accommodate the need for care the municipality was, after five working days, to pay a certain sum to the county for continued care at the hospital. This created an incentive for the municipalities to see to it as soon as possible that the patient in question was moved from the hospital to less costly accommodation alternatives.

Compared with other public areas, the development was dramatic, as the economic crisis in other areas brought with it relatively reduced budgets for service, as the same time as the proportion of the municipal budget that went directly to financial support increased (see diagram 9). It is therefore difficult to explain the increased costs in the early 1990s, considering the economic crisis. It is easy to assume that the Ädel Reform initially had the effect that both municipalities and counties were given increased budgets compared to the size of the activities, even beyond the extra government subsidies that were paid in connection with the transfer.

110 Johansson 2005 p 9

111 Johansson 2005 p 9

112 Johansson 2005 p 9

113 Swedish: "Det kommunala betalningsansvaret"

If the municipalities and the counties were compensated just for their actual costs the reorganization of the tax structure would lead to an unchanged or even reduced direct taxation by the counties and municipalities (part of the costs were intended to be covered by increased government subsidies). If this had happened, it should be possible to see a largely uniform tax increase in the municipalities that belonged to the same county in connection with the reorganization of the tax structure.¹¹⁴

If a comparison is made between how the care costs have developed during this thirty-year period, compared to other welfare services, it will be observed that these costs have increased more slowly than for example child care, which between 1970 and 1990 increased by 450 percent, but at the same time a little faster than the cost for the schools. In connection with the Ädel Reform which was implemented on January 1, 1992, the adjusted municipal costs clearly decreased (see diagram 9). The method for doing the calculations were changed between 1992 and 1993 in connection with the reform but it is hard to determine whether the changed calculation method is the whole explanation. If a comparison is made with the transfer of responsibility for schools, which took place at the same time, no corresponding cost reduction is found.¹¹⁵

The Ädel Reform has as a consequence that the municipalities made different judgment calls as to how the Elder Care should best be reorganized and about how to distribute the resources. As a consequence of this, the costs vary between the municipalities. Variations between years also appeared. The explanation as to why can probably be found partly in that the municipalities experimented with new solutions, partly in that the new methods for Elder Care required new investments, in particular in buildings. In the case of Elder Care, Ericsson, on the other hand, claimed that one of the reasons for implementing the reform was to strengthen the municipal self-government and open up the possibilities for new diverse local solutions.¹¹⁶ That many – not to say most – municipalities elected, in connection with the reform, to move away from the old model with care home facilities towards smaller care units suggests that this was the case.

114 Twaddle (1999) p 93, 211, writes that the municipalities did not receive full compensation for their costs for the activities that they took over. "*The Ädel Reform shifted one of the areas of rapidly expanding cost from the counties to the municipalities. In neither instance was there a transfer of funds corresponding to the magnitude of the shift in responsibility*". He is of the opinion that the municipalities could not, as an alternative, compensate themselves by increasing taxes because of the municipal tax increase ban (p 116). Twaddle, however, gives no source for the statement that the municipalities did not get full compensation for their costs (i.e. that the counties won in the negotiations), nor to the fact that the municipal tax increase ban would have prohibited the municipalities from financing the activities.

115 It is worth noting that the municipal costs for social protection, i.e. cash grants and the like, increased significantly in connection with the 1990s crisis. This can explain some of the initial cost reduction within Elder Care. As the municipal tax increase ban was in force the municipalities could not handle the increased costs by raising taxes (it is also likely that increased taxes at least over time would have resulted in an increased number of recipients for social care as it would increase costs to hire and that it would have reduced the economic margins for those that had jobs) and because of this, tax increases would have been avoided by the municipalities.

116 Ericsson interview 2008

Concerning schools, the pattern is different, something that can be seen from diagram 9; for one thing, the transfer does not by itself give a clear cost reduction for the schools, for another, the differences between municipalities rather decreased than increased (Lakomaa 2008). Elder Care, unlike the schools, are technically a voluntary activity for the municipalities, even though it is stipulated in municipal law that that care should be offered to those that need it. This meant not only that the expenses in this area are given lower priority, but it also means that there is more room for experimentation and local solutions. In connection with the transfer of responsibility for the schools, it was distinctly stated that the transfer of primary responsibility should not bring any changes in content or result in differences between different municipalities or parts of the country. On the contrary, the Minister of Schools expressed the opinion in this case that the control and the follow-up of achievement of goals should be more extensive after the reform.

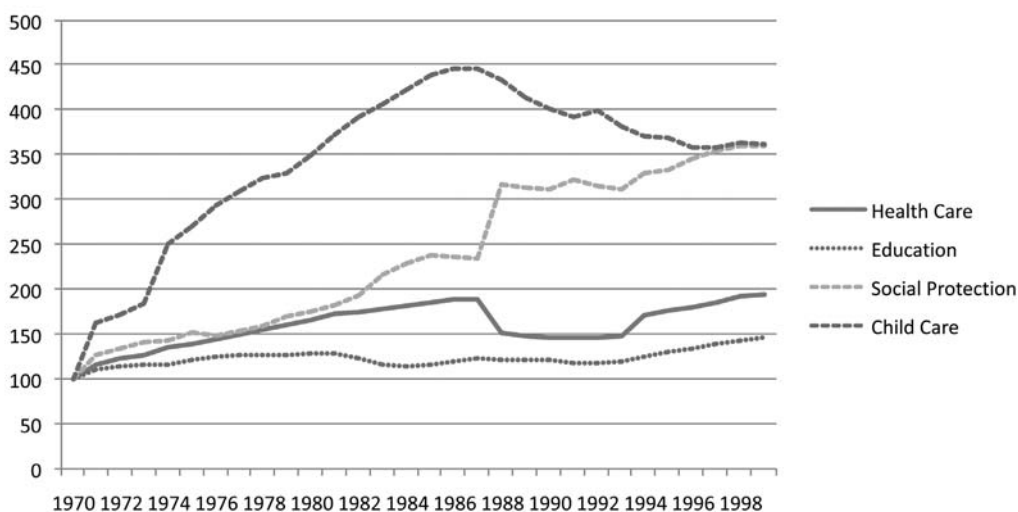


Diagram 9. Municipal expenditures for social protection (mainly cash grants), municipal education¹¹⁷, health and medical care (manly for the elderly but also for the handicapped), and Child Care, adjusted for the transfers of primary responsibilities. Year 2000 prices Index 1970=100. Source: Statistiska Centralbyrån, Tidsserier för offentlig sektor.

In summary, the Ädel Reform had a clear impact both on cost development and the direction of the activities, effects that can not be explained by the crisis in the 1990s.

117 As the high-school was extended by making the two-year study programs into three-year study programs starting with the 1994 school year, the costs should have increased, but they did not

8. Approaches to Explanations

The historic description of the road up to the Ädel Reform (transfer of elder care from counties to municipalities) has room for a couple of general questions that it is interesting to develop further.

The length of time for the process

The cost development trend break

The process up until the Ädel Reform has as its distinguishing characteristic that it took a very long time, several decades. As early as when Gunnar Sträng was Minister of Social Affairs in the middle of the 1950s, there were proposals in that direction and the development thereafter made the climate even more favorable for such a reform. The first of these changes was the reorganization of Swedish municipalities, which in one swoop made the municipalities considerably fewer and larger. One of the reasons behind this municipal reform was that the municipalities needed to become larger to be able to offer different kinds of public service that they had difficulty running efficiently on a small scale.

It is also possible to draw a parallel with the build-up of Child Care. Subsequent to elder care having expanded considerably from the middle of the 1960s and up until the beginning of the 1970s, the large expansion of public activities fell on Child Care. This new area, however, came to be a wholly municipal concern, in spite of the fact that the schools fairly shortly before this, in 1972, had been transferred to the national government. The care for children of pre-school age was thus a municipal responsibility, while the schools were the responsibility of the national government, and elder care a county responsibility. This, however, was not true in the entire country; in the municipalities of Gothenburg, Malmö and Gotland, both health care and elder care were municipal responsibilities.

The Social Democrat government at the time was at the same time of the opinion that welfare policies ought to be organized so that the national government had responsibility for income security (i.e. transfer payments), whereas the municipalities were responsible for producing welfare services.¹¹⁸ Also, concerning this area of activities, there were no deep ideological disagreements, which there were in other areas which had been the object of reforms during the same period. Regardless of whether the Parliamentary majority was with the center-right block or with the socialists, it is likely that it would have been possible to assemble a majority for the transfer of responsibility for elder care any time during the period 1970-1990.

118 Carlsson interview 2007, Åberg interview 2007. Regarding Child Care, both Åberg and Carlsson describe it as extra controversial, because Lisbeth Palme (wife of Prime Minister Olof Palme) was deeply committed to this issue and because of this, it was hard to get savings in this area past the Prime Minister. This picture is confirmed by Feldt (1991), who writes that it was almost taboo to talk about the possibility of savings or increases in the efficiency of Child Care. In spite of this difference, it is clear that elder care and Child Care came to have similar cost developments.

In view of the fact that there was a wide-spread consensus about the desirability of a change of the Ädel Reform kind, even if it was possible to argue about details, the process is a poor fit with the inertia model for political decision making which was used by Borg (2004) to analyze the pension decisions and the gradual removal of the home construction subsidies. The reform process was, concerning elder care, not having inertia, but it took a long time.

Nor is it possible to find any external event or any cost crises that sparked the change; instead it went on at a moderate rate during four decades. That also makes Kingdon's (1995) models concerning political decision making not applicable. The "window of opportunity" sought by him was, in that case, open between the mid 1950s and the beginning of the 1990s. Possibly, it could be argued, in terms of that the window was indeed ajar during the entirety of the described period, but that it was not until the Ädel Delegation (the group studying the issue) got the composition it did – with the municipalities represented by influential Social Democrats – that the window was flung wide open. It should be noted, however, that the level of conflict was unusually high during the period during which the Delegation was active. The Delegation can thus, seen from this perspective, rather have delayed a solution. The alternative with a deal in Parliament before the representatives for municipalities and counties had come to an agreement was there all the time. This was the way previous organizational reforms had been decided; for example, no regard was given to the municipalities when, in 1969, the bulk of the "Comprehensive School" reform was decided, and the schools were made a responsibility of the national government.¹¹⁹ Another possibility is that the demands from the Liberal Party – for each patient in long-term nursing care to have his or her own room – opened up a solution where the government added resources to make an agreement possible. This way, the Social Democrat government could give as a reason for the additional money to long term care – that it was necessary to get the Liberal Party to agree to the reform. The possibility of having an agreement that reached across the aisle should thus have been the situation that opened the window.

Organizational reforms do not have to be slow. Sweden, during the latest half-century, implemented a number of far-reaching reforms. First came the reorganization and consolidation of the municipalities during the 1950s and 1960s, then the transfer of the police force to the national government during the 1960s, the transfer of the schools and the reform going to a 9-year comprehensive school during the 1950s and 1960s, the court reform in the 1960s, and finally the municipalization of elder care and the re-municipalization of the schools in the 1990s. Of these, the municipalization of the schools and of elder care (from the national government and from the counties, respectively) which distinguished themselves by, despite a wide-spread consensus about the desirability of the decisions, having a decision process that comprised decades.

The resistance against the Ädel Reform was to be found primarily outside Parliament, and primarily from the Association of Swedish Counties. The main arguments for keeping elder care as a county responsibility was mostly that with a

¹¹⁹ The decision was made in 1969 but was not implemented until 1972/73.

transfer to the municipalities, it would not be possible to guarantee the medical quality and that a transfer of such a large part of the activities as elder care would be a step towards abolishing the counties as administrative entities.¹²⁰ The latter is not surprising, considering that for example Lars Tobisson (from the Moderate Party) and Lars-Eric Ericsson (from the Social Democrat Party) shared the opinion that the counties ought to be gradually abolished.¹²¹ In Parliament, there was, however, no wide-spread support for this opinion, which made the fear of it fairly unfounded. Concerning the fears that municipal elder care would bring with it that the medical quality would be compromised, there was precedent cases to be studied, as the municipalities were already handling elder care in the municipalities of Malmö, Gothenburg and the Municipality of Gotland. Thus, it was not a matter of who was the responsible party, but a question of organization. Here however, it should be mentioned that several of the central actors bring out this comparison because they are of the opinion that the comparison has problems because they argue that in those municipalities, “mini-counties” had been organized within the municipalities to handle the care issues.¹²²

The research issues under consideration can be attacked from several different directions, and with several different theories. According to Institutional Theory (North 1990, 2005) institutions are the restrictions that people create to describe the methods of human cooperation. The institutions can be formal, that is be rules that are deliberately formed by people – for example, laws, regulations and contracts – or informal, that is rules that are shaped without a clear agent of creation, for example conventions and traditions. A central concept within institutional theory is *path dependence*. Path dependence means that our alternatives between which we choose today are determined by earlier decisions and events, and that has as a result that we often follow the path that has been started, that is institutions are self-reproducing. Non-psychological explanations for path dependencies are for example *network externalities* (David 1985, Katz & Shapiro 1985) and ratchet effect (Kingdon 1990).

Network externalities mean that the utility of an alternative is dependent on how many others have already chosen this alternative. To choose an operating system for a computer, the operating system already has many users is to be preferred because the availability of software is so much larger. In the same way, the utility of having a fax machine depends on how many others have one, if you are the only one who has one, it is worthless (Liebowitz & Margolis 1990). David described (1985) how a sub-optimal standard can remain the standard purely by the fact that it has been in existence for a long time, and people have adapted to it. His example is how the keyboard layout QWERTY has survived from the time of typewriters in spite of the fact that it is not optimal, because it would cost too much for the users to learn a new fingering. Even if this particular example has been criticized (Liebowitz & Margolis 1990) the presence of standards are often central to explain economic development. We can see clear path dependencies within the area of elder care and as a tool for analysis, institutional theory has value. As we shall see, these path dependencies can also have psychological causes.

120 Ericsson interview 2007

121 Gennser interview 2007, Ericsson interview 2007

122 Ericsson interview 2007

On the other hand, institutional theory is hard to use to explain why the reform happened when it did; the institutional change did not take place until after the change of the responsible party. That actors, in this case representatives for municipalities and counties, attempt to change the institutions to their advantage is natural. Thus, institutional theory can explain the motives for why there was an interest in implementing the reform, but for an explanation of how the decision process worked, some other theory must be used.

For example, there is no institutional change that can be said to have sparked the actual decision; the organizational change that followed the decision, on the other hand, came to change even the institutional framework. An institutional approach can thus provide an answer as to why the change of responsible party came about (even if the answer becomes the same as with a Rational Choice approach) and why the reform came to influence the cost development – the reform did influence the institutional framework (even if that does not say anything about in which direction the change on the cost side would go). It can, on the other hand, hardly be used to explain how the process worked and why the decision was made at the actual time that it was.

From a classical rational decision model, for example of the kind used by the Rational Choice school or in neo-classical economics, it is hard to explain both why the reform took such a long time and the results of the reform. The decision was about a change in the responsible organization, and the motive for the change was not to change the organization delivering care. Traditional theory cannot explain why a change in the responsible organization should lead to both reduced costs and an increased variability of the costs. However, such an explanatory approach can go far when the issue is explaining why a change took place (in this case because the majority in Parliament all the way back to the 1950s shared the opinion that a change of responsible organization was desirable).

8.1 Economic-psychological theories

The classical rational decision model has been challenged by researchers in economic psychology. These researchers have observed that people's behavior deviates from that of theories about rational behavior in economic sciences. A central theme has been negative deviations such as that people do not always maximize the long-term benefit when they make a decision, but instead are governed by short-term considerations, by psychologically easily accessible information and by their emotions. Economic-psychological theories are also used to explain how people solve conflicts. It should be noted that this paper does not try to test whether these theories are correct. The ambition is instead to see if any of the predictions that these theories give do indeed match the actual outcome, and also, if possible, to see whether the decision makers themselves may have considered these effects when they have worked on getting any particular decision accepted by Parliament or when they shaped the reform.

The economic-psychological theories that are used in this paper can be sorted into four main categories: reference point theories (adaptation level), mental accounting, the prospect theory and Proximity Effects (social impact theory). These can be said to constitute the fundamental concepts within economic-psychological theory (Belsky & Gilovich 1999).

8.1.1 Mental Accounting

Mental accounting means that people divide current and future resources (money) into different (explicit or implicit) accounts depending on their origin, when they will be used and for what purpose. Through this method, gains and losses will be experienced differently depending on which account they impact, and this influences consumption decisions (Thaler 1980, 1985, Kahneman, Knetsch & Thaler 1991). The propensity to save versus to consume differs between different mental accounts. For example, the propensity for saving is large for capital accounts and for lump sums, but small for income and consumption accounts (Thaler 1980).

Thaler (1985) exemplifies with a couple that has saved 15 000 dollars to be able to, five years later, buy a vacation cottage. The money exists in an account that produces 10 percent interest per annum. At the same time, they buy a car for 11 000 dollars which they finance with a three-year car loan running at 15 percent interest per annum. The money in the savings account and the money from the car loan are found in different mental accounts and are evaluated separately, so instead of using the money from the savings account to buy the car, they borrow money at a higher interest rate than the yield on the savings account.

Mental accounting can have different effects depending on how the accounts are defined and how they are combined. If we have two outcomes, x and y , and evaluate them together as one account, that is according to the formula $v(x+y)$, i.e. $v(x)+v(y)$, this is defined as being “integrated”. If, on the other hand, we evaluate them separately, this is defined as being “segregated” (Antonides 1991). If both outcomes (x) and (y) are positive, segregation will produce a higher total value, because the evaluation function is concave. “*The moral of this is not to wrap all Christmas presents together*” (Antonides 1991). If, on the other hand, both outcomes are negative, integration should be used because the total disutility is then lower. This phenomenon could for example be what is behind that many people tend to spend more when they pay by credit card than when they pay cash. Since the credit card bill adds many small expenses into one large one, the experienced loss is reduced by the integration of the accounts, at the same time that the utility of the different purchases remain segregated.

Another case is when one outcome is positive and the other is negative, but their sum is positive. Integration then results in the negative outcome being extinguished by the positive outcome, and the result is viewed as a gain. For example, this can explain why taxation at the source (as in payroll deductions) produces less dissatisfaction than if the taxes have to be paid by the taxpayer. The payroll deduction system makes the income and tax accounts integrated. If, on the other

hand, the situation is one where one outcome is positive and the other is negative, but where the sum is negative, it is not obvious whether integration or segregation will be used. If one outcome, x , is small compared to the other, y , a so-called silver lining effect can materialize by segregating the accounts. Silver lining means that some of the suffering that a bad outcome produces is mitigated by the happiness that is given by the positive outcome. Thaler (1985) shows with an example how this might work.

Mr. A's car was damaged in a parking lot. He had to spend \$200 to repair the damage. The same day the car was damaged, he won \$25 in the office football pool.

Mr. B's car was damaged in a parking lot. He had to spend \$175 to repair the damage.

Who was more upset?¹²³

When the question was posed to students in an experiment, 19 answered A and 63 answered B, while 5 saw no difference. In this case, there was clearly a silver lining effect. The same effect can be used in a business context, for example when the seller gives a discount. The discount is often small compared to the price, but is used to reduce the suffering of having to spend money. Mental accounting is connected to several different psychological phenomena which concern human decision-making, among which are status-quo effects or endowment effects, omission bias and sunk cost effects.

The *endowment effect* means that people tend to over-value things they have (but might lose) and undervalue things they do not have (but can obtain). Thaler (1980) gives an example: Mr. R in the late 1950s, bought a case of good wine for five dollars a bottle. A few years later, the wine merchant offered to buy back the wine for 100 dollars a bottle. R refused, in spite of the fact that he never had paid more than 35 dollars for a bottle of wine. If he instead had been offered a choice between 100 dollars and a bottle of this wine, we may assume that he would have chosen the money, as he never had paid more than 35 dollars for a bottle of wine. By the fact that he already owned the bottle, he was not willing to give it up even if he would not have bought it at that price.

Kahneman, Knetch and Thaler (1990) performed a classic test of this effect by showing that people who randomly had been given a mug demanded a significantly larger payment to sell their mugs than those who also randomly had been chosen were willing to pay to buy the mugs in question. Samuelson and Zeckhauser (1998) call the same effect a status-quo effect as it means that status quo is preferred to alternatives that consist of change.

Omission bias means that the decision maker prefers an alternative that requires no action to one that does require action; the result is the same as for the status-quo effect. A test for this effect was performed by Hartman, Doane and Woo (1991) and used electric power customers in California. The customers were asked how they would consider different combinations of service and prices where some combinations were said to be the status quo. Regardless of whether it was a combination of

123 Thaler 1985, p 204

a low price and little service or a high price and lots of service, most people chose not to change (see also Kahneman, Knetsch & Thaler, 1991). Omission bias can also be connected to the fear of being held responsible. He who actively chooses to do something is much more likely to be held responsible than somebody who passively watches and lets things happen. A classic political example is the argument against seeding hurricanes.¹²⁴ Even if the total amount of damage would be less if the hurricane was seeded, it would be possible to hold somebody responsible for the actions that led to the damages. Potentially, somebody can be sued for the damages that occur by a hurricane changing directions caused by seeding whereas a hurricane that follows its natural path is act of God. It is possible to argue in terms of that damages caused by acts of omission are seen as foregone gains, whereas damages caused by acts of commission are not. Kahneman and Miller (1986) have also shown that acts of commission produce a larger amount of regret than acts of omission if the outcome is negative. Another observation is that the willingness to pay for the removal of an existing risk is often less than the willingness to pay for not having to accept a new risk. Omission bias can also be present in decision situations where the outcome of the alternative not chosen will never be known. For example, people can be unwilling to vaccinate their children even though the risk of death from the vaccine is lower than the risk of death from the disease against which the vaccine would have offered protection (Ritov & Baron 1990).

The sunk *cost effect* means that we base decisions on other decisions previously made and not on the consequences of the decision we are facing. Thaler (1980) explained the sunk cost effect with loss aversion, combined with integration of mental accounts. If you have already spent nine million on an investment, you might as well spend another million to get something. The extra million is then put in relation to the outcome of the whole project, and can be seen as reasonable, even if the value of the whole project does not reach ten million (but is more than one million). If you do not put in the extra million, you will experience the nine million already spent as lost, which you want to avoid in spite of the fact that an alternative use of the last million could have given a higher payback.

The sunk cost effect can also be explained with “regret”, as according to Arkes and Blumer (1985). We feel more regret if we invested nine million and got nothing back than if we invested yet another million and received something. They also describe how the prospect theory predicts that people take risks in a bad situation, with the goal of regaining earlier losses or to regain sunk costs. Sunk costs can also influence decision making through “*escalating commitments*” (Staw 1976, Schaubroeck & Davis 1994, McDermott 2004).

Individuals who are not responsible for an original policy that failed may be more likely to stop the policy, as opposed to putting further resources into it. Those responsible for the policy appear to want to recoup their losses through an escalations strategy and to recover their sunk costs from the previous effort more than outsiders do.¹²⁵

124 By airdropping chemicals from airplanes, it is possible to produce rain, and thereby make for example hurricanes use up their energy content earlier and change their paths and thus hit areas that are less populated.

125 McDermott 2004, p 300f

Both the sunk cost effect and the omission bias produce what in economic history is usually called path dependencies: that is we continue on the path begun, because earlier events and decisions limit the alternatives between which to decide today. Network externalities are a common rational explanation to path dependencies, the ratchet effect is another. Network externalities have been described above (see page 159) and ratchet effects are a political science based explanatory approach which describes that some decisions become politically irreversible. For example, it can be much harder to raise speed limits once they have been lowered than to stop a lowering, however small. Those who want to raise the limit will immediately be accused of wanting to increase the number of traffic fatalities. The reasons for the irreversibility can be different factors, including psychological phenomena such as reference points or omission bias. The latter because whoever makes the decision would risk being held responsible – at least indirectly – whereas the gains from the increased limit would not be traced to any one individual decision maker.

8.1.2 Reference Points

In decision situations, *reference points* have an important role. How we value some things depends on which reference point (within a mental account) that we use. This can express itself in different ways. According to the classical Weber-Fechner model, the intensity of a sensation is proportional to the logarithm of the intensity or the strength of the stimulus that causes the sensation. This means that we will react more strongly to for example an increase in the price of an item from 10 to 20 than from 20 to 30, in spite of the fact that in the latter case we will have less money left after the purchase (Gunnarsson, Wahlund & Flink 2000). Another variant is adaptation level or context effects (Helson 1964). This means that our subjective judgments are relative to the level that we are used to. We would for example perceive a tennis ball that weighed 4 ounces as heavy, but a football weighing 4 ounces as light.

By defining these reference points, different results can be achieved. This is commonly called “*framing*”. The use of “cash discounts” or “credit card surcharges” in stores means that the merchandise has two different prices, one if you pay cash, another if you pay by credit card (Thaler 1980). The customers experience the presence of a cash discount as a gain, whereas they experience the credit card surcharge as a loss. Because the value function is steeper for losses than for gains, the customers will, however, be more likely to use credit cards if they perceive it as foregoing a cash discount (that is forgoing a gain) than if they perceive it as that they pay a credit card surcharge (that is accept a loss). If the merchant gains more by his customers paying by credit card, he will thus call the difference a “cash discount” and vice versa. The importance of framing also means that the setters of agenda and political entrepreneurs have an important role as they can decide how the alternatives are presented and they can therefore position them in different ways on the value function depending on what they want to achieve.

8.1.3 Prospect Theory

Prospect Theory (Kahneman & Tversky 1979) is based on the fact that people care more about changes (within mental or actual accounts) than about totals, levels or states, and prospect theory describe how people make decisions in situations that include risk and how they value potential gains and losses. According to Prospect Theory, the value function is concave for gains and convex for losses. This leads to loss aversion for gains and risk seeking for losses. Additionally, the value function is in itself loss averse, that is the function is steeper for losses than for gains.¹²⁶

The implications of this theory is for one thing that people pay more attention to losses than to gains, and for another that change is more important than level or state. The latter phenomenon is because there is a tendency to define changes as disimprovements. Experiments have also shown that changes that are near to the reference point are assigned a bigger weight than changes that are further away from it. Additionally, there is a tendency for people to overestimate small probabilities at the same time that large ones are underestimated (Kahneman & Tversky 1984). Experiments show, for example, that people overestimate the risk of dying in air plane crashes, but underestimate the risk of dying as a result of diabetes (Slovic 2000). According to Wahlund (1994) small probabilities are overestimated more strongly in situations of potential loss than in situations of potential gain. This can be assumed to result in that a change becomes difficult to implement because negative outcomes from the change will get more weight. All this affects how people act in decision situations.

Bazerman and Neale (1991) have described how Prospect Theory affects negotiations. If negotiator A believes that each concession he makes is a loss to him or to the interests that he represents, this will result in that the probability of achieving an agreement is less than if the negotiator believes that each concession made by the other party, negotiator B, is a gain for A:

Negotiators bargaining over losses tend to make fewer concessions, find fewer integrative solutions, and more often fail to reach agreement than negotiators bargaining over gains.¹²⁷

It follows from Prospect Theory that the concessions that give the most effect in a negotiation are those that reduces the other party's losses, whereas the least effective ones are those that increase his gains when he is already ahead.

Reference points and the value function according to Prospect Theory also affect how differences between different alternatives are evaluated. The difference between disadvantages tends to have more weight than differences between advantages. Kahneman (1992) describes for example how the difference between two salary offers of 40,000 and 45,000 dollars will be perceived as the difference between two gains by somebody whose present salary 35,000 dollars, and as the dif-

¹²⁶ That people are more sensitive to losses is, however, nothing new, but something that was noted as early as by Adam Smith who in 1759 wrote "We suffer more [...] when we fall from a better to a worse situation, than we enjoy when we rise from a worse to a better" (Smith, 1759 p 311).

¹²⁷ Kahneman 1992, p 297

ference between two losses by somebody whose present salary is 50,000 dollars. As the value function is steeper for losses, the difference between the two alternatives will be perceived as larger for the person with a high salary than for him who has a low salary.

8.1.4 Proximity Effects

Another important field within economic psychology is something we can call *Proximity Effects*. Proximity Effects mean that the decision maker pays more attention to people whom they meet or risk meeting than to people that they will never have to meet when they make a decision. Proximity Effects have been described by Milgram (1963) and by Kilham & Mann (1974), among others. A special field is Social Impact theory (Latané 1991). Experiments done by Latané show, for example, that it is easier to influence somebody in a small group than in a large one, that is we pay more heed to what others have to say in a smaller setting, and that we contribute more in such a smaller setting. Latané showed, among other things, that a group that has eaten at a restaurant gives more tips if they get one check per person than if they get one check for the whole group, and that there were more people who became convinced by the evangelist Billy Graham if they listened to him in a setting with few other listeners (Latané 1981, Latané & Wolf 1981).¹²⁸ Applied to political decision making, this can explain why more consideration of the voters is given at a low administrative level, such as the municipal level, than at the county or national level. This is a well-known phenomenon in politics. Myrdal (1982) reflects that it was harder to make decisions when he was the Mayor of Mariefred than when he was a Member of Parliament, because in the former case he was at a considerable risk of running into somebody who had been affected negatively by the decision.¹²⁹ Even Gunnar Sträng supposedly has thought in terms of Proximity Effects when he pointed out that municipal politicians – in contradistinction to politicians and civil service employees at the Ministry of Finance – often had a hard time standing up against demands from the voters.¹³⁰

128 It can be noted here that the examples described can also be explained by mental accounting in combination with different reference points. The restaurant customers put the tip and the cost of the food in different mental accounts, and they experience it as leaving a bigger tip if the tip as an absolute number is larger. This gives the same result as the proximity effect. This, in turn, can serve as an example of the fact that it is often difficult to isolate which effect that is behind which; this admonishes us to be careful about drawing conclusions.

129 Myrdal 1982 p 86

130 Åberg, interview 2007

9. Analysis

Both the process leading up to the Ädel Reform and its implementation were likely affected by these economic-psychological effects. The drawn-out decision process can be analyzed both as a negotiating process between municipal and county interests and as a process governed by the propensity for change within the national government as a whole. In both cases, an economic-psychological analysis is fruitful.

The municipalities had expressed an interest in taking over all of the elder care (and additionally, gladly, primary health care), while the counties wanted to guard and retain its then current tasks. In case of a potential change of responsible party, the municipalities wanted to get revenue as large as possible from the restructuring of the tax system, at the same time that the counties wanted to retain as much of the tax revenue as possible. There, interest was positioned against interest. There was, however, a wide consensus when it came to describing the problem. Both municipalities and counties, as well as Parliament, were in agreement that the then current organization of activities did not function well.

Here, the question ought to be asked why elder care had not been reorganized earlier. During the ten-year period which preceded the decision about the Ädel Reform, the then current system was discussed and studied several times, for example in the “preparatory study group” for elder care, and in several public studies. That the activities did not work well was pointed out by for example the chairman of the preparatory study group (“*Äldreberedningen*”) Sture Korpi. He was of the opinion that for example one of his main motives to get to a change was to get rid of the “*Älderdomshem*” (“elder homes”, large facilities for the aged), which, according to him, worked very poorly.¹³¹

A reorganization had most likely been in the interests of the counties because it would reasonably had been easier for the counties to argue that they should keep that responsibility if the activities were well handled and cost effective. Well-functioning county elder care might even have brought with it that, as proposed by the chairman of the Association of Counties, Gunnar Hofring, the counties could have taken over all elder care, including the parts that were already handled by the municipalities. To be sure, it would have been easier to reform an integrated elder care system, but from a rational analysis model, it is nevertheless surprising that nothing was done to ameliorate the shortcomings and that the activities were not adapted to the demographic changes to any reasonably high degree. Such changes had also probably been able to limit the cost escalations. The thrust of the activities after the reform was changed such that a larger amount of resources were spent on older and sicker users, to the detriment of those younger and healthier. These changes were most likely necessary, sooner or later, considering the aging population.

131 Korpi interview 2008

The drawn-out process could be caused by for example status quo effects, omission bias or sunk cost effects. The organizational model that was in place was the reference point and the status quo alternative. Changes compared to this alternative would thus mainly be seen as disimprovements because any negative consequences of the change (and anything that had to be foregone by abandoning the then current system) would be overvalued, while the positive effects (and the gains from abandoning the then current system) would be undervalued. Not to do something would thus protect the decision maker from criticism. If changes had been implemented that in some way had been perceived as failures, that too had risked getting criticism. This conforms well with the theory of omission bias. Obviously, the same is true for the actions of those politicians at the national level who decided about the reform and the effect can in the same way explain their resistance to change. Additionally, this can have been strengthened by that people tend to overestimate the probability of a negative outcome.

An alternative explanation is given by sunk cost effects. If you have spent a large amount of resources on one model of operation, the sunk cost effects can lead to that you try to solve any problems by adding more resources instead of changing the model of operation, this with the goal of not losing investments already made. This can also be analyzed in terms of escalating commitments, yet an effect of loss aversion (Kahneman 1992). According to this theory, those who are responsible for a failed strategy will rather want to continue on the path they are already on and add more resources than to admit that the strategy was wrong. In the case of elder care, politicians both at the national level and the county level would have been at risk of being governed by escalating commitments.

At the same time, the massive cost increases during the 1980s can probably be said to have contributed to that the changes were in fact implemented. If the costs had continued to increase at the rate that they did during this period before the reform, the costs by year 2002 would have been close to 50 percent higher than what they in fact were (see Diagram 7). This most likely contributed to that the reform did happen. If the future costs were used as a reference point the alternatives that provided change would look more attractive. This, together with the extra funds that were added at the negotiations are, if the implications of the economic-psychological theories are considered, most likely the keys to the solution to the problem. When the status quo alternative was eliminated thought the change of reference point, Assistant Minister of Social Affairs Lindqvist could then reframe the whole process in terms of change, and thus avoid being locked to the status quo alternative.

Political changes are often combined with added funds as bait, which would not have been needed in a world of neo-classical actors. This was also the case in connection with the Ädel Reform. Among other things, the government added extra funding from the national treasury in connection with the reform, something Minister of Finance Feldt called "lubricant".¹³² If we apply the reasoning about reference points and loss aversion to the change of responsible entity we can envision the following explanation: The costs that the municipalities took over can be

132 Songur 1993 p 5

assumed to be seen as a loss and the tax revenue that they took over can be seen as a gain (here we do not consider the fact that a large field of activity can be seen as an advantage in itself, e.g. by giving political prestige). For the counties, the reverse is true. The loss of tax revenue becomes a loss and the lost expenses become a gain. The larger the cost, the larger the overcompensation would be demanded (though the reorganization of the tax system or through direct funds from the national government).

In the negotiations, the counties, (quite regardless of any economic-psychological effects) had an interest in getting the costs – as shown in the accounting – down as much as possible while the municipalities gained by having them exaggerated. If both municipalities and counties were allowed to overcompensate themselves in connection with the change-over, thus a change could have become acceptable for both parties. This was indeed what happened; both the municipalities and the counties increased their total revenue relative to the expenses when the responsibility for elder care was transferred. This happened primarily because the municipalities in many cases raised the income tax more than what the transfer of responsibilities would have required, while at the same time many counties did not reduce the taxes to the same extent. The calculation of the amount of the tax shift was done without regard to any potential for increased cost effectiveness. The municipalities thus may have obtained additional economic gains by the fact that after they had taken over the responsibilities, they could achieve further increases in cost effectiveness which means that they could have overcompensated themselves even in those cases where the tax reform was done entirely according to the principle that the total tax burden remain constant.

Economic-psychological effects may also have influenced the way the decision was made. Politicians can be assumed to be aware of which obstacles – psychological and other – that there are to push a decision through and can be assumed to consider how people function in decision situations. If we study how the decision to transfer the responsibility was achieved, we can find some examples of how such psychological effects were used or taken into consideration. To overcome the resistance to change, the proponents of the reform, primarily Assistant Minister for Social Affairs Bengt Lindqvist, phrased the alternatives as different alternatives for change. A municipalization of elder care was put as an alternative to transferring both elder care and all primary health care to the municipalities. This formulation of the alternatives created new reference points and any alternative denoting leaving things as they were was not given. Thus, the effect of omission bias was also eliminated. The presentation of the question also excluded other alternatives, for example the proposal from the chairman of the Association of Counties, Gunnar Hofring, to instead move all elder care to the counties. It was not a given before the fact in which direction the transfer should be made, from counties to municipalities or vice versa, but by establishing the alternatives between which to negotiate, the question that remained was which activities the municipalities should take over and which should be retained by the counties. The status quo alternative was thus completely defined away.

However, it should be pointed out that the Social Democrats, like to a varying degree the center-right opposition parties, were supporters of the idea that the welfare state should be shaped such that the national government would handle income protection (transfer payments) while the municipalities should produce welfare services (this, too, can be seen in terms of different mental accounts), which made it easy to frame the question in the way it was done. The reference point against which all other proposals were evaluated was thus a municipalization. Those who resisted the transfer of responsible party, primarily the Association of Counties and the Center Party instead tried to frame the question such that the municipalization of elder care was connected to the issue of the existence or non-existence of the counties as administrative units.¹³³ By moving the reference point it would become more difficult for the counties to make concessions. Thus, it would also become more difficult to achieve a solution (the counties were satisfied if everything continued as earlier, so a breakdown in negotiations would have served the purpose of the counties). Through the intercession of the board of Social Democrat Party ("*partistyrelsen*"), and its declaration that it would not accept the proposal from the Association of Counties, the negotiating strength of the counties was seriously weakened. Instead, the negotiation came to be over which activities should be transferred to the municipalities, and how much compensation this would entail. Here, the extra funding from the national government most likely came to untie the knots.

The extra government funds can also be seen as a silver lining. To the municipalities, the funding would have been some compensation for the increased duties; for the counties a compensation for the decreased tax revenue. This is, however, not crystal clear. It is more reasonable to assume that the extra government funding instead served as a compensation to allow the counties to overcompensate themselves when the tax structure was reformed. It was, after all, the counties that were the part that was hard to persuade.

That the municipalization brought with it an increased awareness of costs can be explained with mental accounting, as well as with reference points. When the counties were handling elder care the costs for elder care were integrated with other costs to the counties. This made it difficult to know exactly what elder care did cost. When the decision about municipalization was made, the municipalities and the counties were tasked with agreeing about which activities were to be taken over and how large the costs were for these activities. When the activities were transferred to the municipalities, they thus were separated from other municipal activities and were given clear price tags.

Such a work-through of the numbers, by itself, would probably have led to the discovery of some less well spent expenses. A clear result of the transfer of responsibility was that the nursing homes were phased out. The municipalities were of the opinion that the nursing homes were antiquated and inefficient. To the counties, the nursing homes had been a sunk cost, which can serve as an explanation as to why they had not been phased out when the counties were the responsible party.

133 Berg, interview 2007

As the investment in nursing homes was a sunk cost, the same result should – in the absence of sunk cost effects – have resulted in that they would have been phased out even if the counties had remained as responsible parties..

Further, there was obviously a large potential for cost cutting by increasing the efficiency within elder care; this could have been done even without transfer of responsibility. As a practical matter, the Ädel Reform would be used to break old patterns and rebuild the organization from the ground up. Central actors such as the chairman of the Association of Swedish Municipalities say, after the fact, that this was a reason to drive the reform forward. As long as the counties had the responsibility, changes were not possible.¹³⁴ The changes of the focus of the elder care that did in fact happen, among other things the abolition of the nursing homes, and the changes of the consumption patterns, among which the transfer of resources from care for younger elderly to care for older elderly was not dependent on that a certain responsible party was handling the activities, but was made possible by the transfer of responsibility.

A transfer of responsibility can thus bring with it large changes regarding how the activities are organized. Changes can be easier to implement because the new responsible party is not locked into what has been done earlier. In connection with the Ädel Reform, there were also considerable changes. An approach to explanation based on traditional neo-classical economic theory with rational actors could not give an explanation for the fact that a transfer of responsibility would bring with it any changes to the content of the activities. In this case, it would merely have been a book keeping issue.

As the transfer came to influence the mental accounts of the decision makers, it also came to influence the prioritizations. A municipality which, in connection with the Ädel Reform had a cost increase of 20 percent, but also a revenue increase by the same amount, would not necessarily have wanted to use the money specifically for elder care, but could have seen other pressing needs. That every municipality would have had the same identical preferences as the counties to which they belonged regarding the priority of elder care compared to other areas of expenditure is, on the contrary, extremely unlikely. Nor should the extra funding which was given to the municipalities in connection with the reform have influenced the expense level more than, possibly, temporarily, as this was a one-time funding.

The Proximity Effect is also a phenomenon that can explain why there was a break in the cost development curve in connection with the municipalization. If you assume that elder care at the time of the Ädel Reform generally was seen as less of a priority than other municipal expenditures such as the schools or social protection (that is cash welfare payments) and was therefore given a lower priority in the budget, at the same time that it was viewed as more of a concern to use the scarce resources to help the oldest and sickest, that conforms to the theory

134 Ericsson interview 2007

and to the actual outcome.¹³⁵ The connection between the level at which political decisions are made and the size of public (i.e. tax funded) activities has been the subject of extensive research, primarily within the Public Choice tradition.¹³⁶ That decentralized political systems have, as a consequence, a lower level of public expenditure can likely partly be explained by Proximity Effects in combination with prospect theory and tax competition.¹³⁷ What the voters lose (the taxes they pay), because of loss aversion, is given greater weight than that which they gain (different forms of public service). If the decisions are made at a political level far removed from the voters, for example at the level of Parliament, this gets less importance regarding which tax and expenditure decisions that are made, but if the decisions are made at a low political level, where the politicians risk running into those that have been affected by the tax increases, the Proximity Effect works as a dampener. Frey (1994) and Vaubel (1996) have also shown that when the tax decisions are made at a low level (or by plebiscite) the tax burden is decreased.¹³⁸ Applied to the Ädel Reform, this can have brought with it that the perceived cost (both for the voters and for the municipal politicians) of the additional taxes that were introduced by the reorganization of the tax system exceeded the perceived utility of the additional municipal service, even if the same taxes and (largely) the same services were present when the counties had the responsibility. At the same time, it can be assumed that the Proximity Effects played a role also regarding prioritizing between different municipal areas of activity.

As a change of responsible party makes it possible to create new reference points and, as described above, break old patterns, there should have been a break in the cost development curve in connection with, or, more precisely, after the transfer of responsibility.¹³⁹ This indeed did happen. The cost development trend decreased after the municipalization.

An institutional approach might have been able to explain why a transfer of responsibility, which is an institutional change, should lead to a change in behavior but has a hard time explaining how the behavior would change. By transferring the responsibility for elder care to the municipalities, the result was a situation where it was possible to make a fresh start and not being locked in by old organizational patterns. The institutional approach is less suitable in this case, because it concerns the organizational change that, when it is decided, is followed by in-

135 In 1991 a total of 195,500 people over the age of 65 had in-home service. In 2002, that figure was 125,200. At the same time, the number of people over 90 years of age receiving in-home service increased (partly because the number of nonagenarians had increased and the proportion of care recipients who were receiving around-the-clock efforts increased from a quarter of the care recipients to closer to half). (Jennbert and Molin 2003 pp 16-17).

136 For an overview, see Mueller 2003, pp 209-229

137 At the same time, the reference point becomes lower because the total amount is reduced.

138 Because of the municipal aggregation during the 1950s and 1960s, the size of the municipalities increased while their number decreased, which meant that the impact of the proximity effect and of tax competition was reduced. This might explain why the municipal tax burden took off not until after the municipal reforms.

139 A certain delay can normally be expected, as it is not possible to turn the activities on a dime. At the same time, it is reasonable to expect that a decided but not yet implemented transfer of responsibility can bring with it a break in the trend because the earlier responsible party changes the activities before the transfer has taken place.

stitutional changes. The causality is thus the opposite. Nor has it been possible to find evidence that the institutional change was anticipated and that within the organizations (that is the counties and municipalities) adaptations were made to that which was coming. On the contrary, there is fairly convincing evidence that if a negotiated solution had not been arrived at – as it was –, the subsequent institutional adaptation would not have taken place or would have happened in a different form. It is quite possible that either Hofring's proposal about a transfer of all elder care to the counties or Ericsson's proposal where the municipalities would take over not only elder care but also all of primary health care, would have been the final result.

10. Concluding Discussion

The Ädel Reform was one of the largest transfers of activity between two political entities that ever have taken place in Sweden. It was also passed with what was largely a consensus and without ideological disputes. A long time, almost four decades, passed from the time when the first discussions about this change took place in central political circles, and the time when the decision finally was made. The drawn out process can be partly explained by the fact that the issue of elder care came to be connected with the issue of the future of the counties as administrative units, partly by inertia in the actual decision-making process that was connected to the disinclination to accept changes. The reluctance to change can in turn be connected to loss aversions, reference points and status quo effects. Change was perceived, rightly or wrongly, as a disimprovement. Even if the center-right opposition in Parliament had no objections to the reform in itself, they did oppose and found a large number of objections to how the process had been handled by the government, and additionally the opposition produced a number of proposals for change or amendment. To buy off on a proposal from the government as it was originally proposed, had for one thing not been in keeping with the role as opposition, for another it would have had a negative impact on their negotiating position; in this manner the loss aversion was activated. The Liberal Party, which made a deal with the government on this issue, was regarded as having a good negotiating position, and among other things, managed to push through extra funding to fulfill the party's election promise about private rooms in long term care. For the Center Party, guarding the interests of the counties was a priority, and they were more seriously concerned about what they thought of as errors in the decision process. That the debate in Parliament became so voluminous can probably be explained by that in connection with the reform a number of other issues connected with health care or elder care were brought in.

The outcome is clear, the costs for elder care had increased at a steady rate all the way back to when the welfare state started to expand in the 1960s, but the trend was broken by the reform. Instead, the cost curve became somewhat more horizontal at the same time that public expenditure as a fraction of GNP increased. The reform also had as a result that the variance increased, both across time and between municipalities. Several important phenomena can be explained here using economic-psychological theories, which show their value as tools within the study of political decision-making. In this case, that is particularly true in two areas; the break of the trend for the cost development and the overcompensation in connection with the transfer of responsibility. By the national government supplying extra funds, it was possible to induce the parties to accept change. Institutional Theory is here insufficient as an explanatory model, as the organizational change preceded the organizational change, and it is not possible to show that the municipalities or the counties anticipated the institutional change. An explanatory approach based on Rational Choice or interest group theory does not take us all the way either, even if it, like institutional theory, and provide important contributions. Nor can such an approach explain why the decision was made, nor can it explain the break in the cost trend that followed the reform. According to these theories, the change

would have been slowed down because representatives for the counties were afraid of losing funding and influence. This is most likely correct and fits well with the fact that that it was position, not membership of which political party, that determined the opinion about the reform. However, these theories provide no answer to the question why the funding for elder care started to decrease after the transfer of responsibility. If it was just a matter of budget and influence, this is not would you would have expected.

Theories that concern political decision-making, such as Kingdon (1990) and Borg's (2004) model for inertia in Swedish political decision-making are not sufficient either, even if they give some valuable contributions.¹⁴⁰ For one thing, here the issue is not, unlike with Kingdon and Borg, overcoming ideological differences. Nor is it possible to see any precipitating factor for the change. Kingdon's window of opportunity was most likely open for two decades. Possibly, it could be said that the cost explosion within the public sector at the end of the 1980s served as a precipitating factor, but this is not sufficient to explain why the decision was made right at the point when it was made.¹⁴¹ Most likely, it is a matter of a continuous process that was brought closer to a decision one step at a time, but where no solution could be obtained before an economic solution was created which made both sides able feel like winners. This explains why extra funding was needed – both through direct funds from the national government and through possibilities of overcompensation when the tax system was restructured – to make this reform happen.

The general conclusion seems to be that traditional models for political decision-making are poorly suited to explain drawn out decision processes where there is political consensus about the final goal, but that theories taken from economic psychology can bring in explanatory power in those cases.

140 The issue of the existence or non-existence of the counties as administrative entities, on the other hand, would most likely fit well into Borg's framework.

141 Also, see Diagram 2. Pierre's (1993) and Twaddle's (1999) explanatory approaches – that the reforms were made to save face for the Social Democrats facing the threat that bureaucracy and inefficiency within the public sector would discredit the whole welfare state – can be wholly disposed of; if this were the case, the Social Democrat government could have pushed through the decision as early as in 1982, when they regained power. They had proposed municipalization as early as in 1979 and they had a Parliamentary majority for a change even without support from the center-right block.

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The Economic Psychology of the Welfare State

Political decision making can be analyzed through a plethora of theories. Here Economic Psychology is used as theoretical framework to analyze decision making, both by politicians and voters.

The thesis consists of an overview of current research; an econometric study of how the voters in municipal elections react to changes in fiscal policy; and two case studies where the transfer of responsibility from one political level to another are studied, namely the transfer of Elder Care from counties to municipalities, and the transfer of the school system from the national government to the municipalities.

It is shown that political actors often take psychological factors into consideration when they design or react to policy proposals. It is also shown the use of a psychological approach can improve the understanding of political decision making, particularly when the processes are complex or involve negotiations.



Erik Lakomaa finished his PhD thesis in economic history at the Institute for Economic and Business History Research and the Center for Media and Economic Psychology at Stockholm School of Economics in 2009. He has a background as a political consultant.

