

## SPECIAL COMMENT

# France's Social Insurance System : challenges but stable Aaa

---

**Table of Contents:**

SUMMARY OPINION	1
CHALLENGES, BUT STABLE Aaa RATINGS	2
FRENCH SOCIAL INSURANCE: A HIGHLY SUPPORTIVE SYSTEM	3
ACCUMULATING DEFICITS ARE EXPECTED TO LEAD TO RISING "SOCIAL DEBT" RISK	4
MOODY'S RELATED RESEARCH	7

---

**Summary Opinion**

The French social insurance system – encompassing the country's unemployment insurance system (UIS) and its social security system (SSS) – is faced with soaring debt levels that will likely double by 2012, as persistent financing deficits over the past two decades have been exacerbated by the financial crisis. In Moody's view, however, this does not challenge the Aaa ratings of the main agencies in charge of financing France's Social Insurance System as (i) the sovereign rating remains their key driver and (ii) France's Aaa rating remains stable despite its public debt ratios being impacted.

- » Moody's rates the three main agencies participating in the financing of the social insurance system, ACOSS, CADES and Unedic, which all have Aaa/P-1 ratings, with stable outlooks.
- » In Moody's view, growing deficits do not have a direct impact on the credit risk of France's social insurance system, whose ratings are viewed as equivalent to that of the sovereign (Aaa, stable). ACOSS, CADES and Unedic will maintain their Aaa/P-1 ratings as long as their missions and status remain unchanged.
- » Although the debt of the social insurance system forms part of France's public debt, an anticipated rise in debt is unlikely to be sufficient to impact France's Aaa sovereign rating, at least in the medium term; as a result, the Aaa rating of France's social insurance system remains unchallenged.

---

**LONDON** 44.20.7772.5454

David Rubinoff	44.20.7772.1398
<i>Team Managing Director</i>	
David.Rubinoff@moody.com	
Lucie Villa	44.20.7772.5326
<i>Associate Analyst</i>	
Lucie.Villa@moody.com	
Arnaud Mares	44.20.7772.5390
<i>Senior Vice President</i>	
Arnaud.Mares@moody.com	

---

**MADRID** 34.91.310.14.54

Sebastien Hay	34.91.702.6635
<i>Vice President-Senior Credit Officer</i>	
Sebastien.Hay@moody.com	

---

## Challenges, but stable Aaa ratings

### Financial pressure does not threaten Aaa ratings of social insurance agencies, viewed as credit linked to the sovereign

The three entities that play a key role in France's social insurance system, CADES, ACOSS and Unedic, have the same Moody's rating as that assigned to the French government (i.e. Aaa) based on the state's commitment to honouring these entities' debt obligations, which is not meaningfully different from its commitment to honouring its own financial obligations.

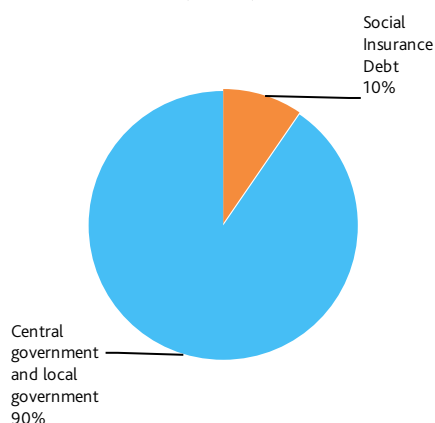
This view is underpinned by (i) the nature of the legal arrangements that bind the state and social security institutions; this is inherent in either their EPA (*Etablissement Public à caractère Administratif*) status (in the case of ACOSS and CADES) or in the form of a contractual long-term relationship (in the case of Unedic); (ii) the deep involvement of the government in the operation of social insurance schemes; and (iii) the critical role that social insurance institutions play in the delivery of the government's social policies. In the near term at least, Moody's envisages that the government would extend its full support, in one form or another, to CADES, ACOSS or Unedic if it were required.

Moreover, any rating assessment of the social insurance system needs to also take into account the government's own balance sheet; some social debt is included in the central government's debt accounts. More generally, social debt is included in the broader aggregate of government debt (the Maastricht definition of public debt), which is used by Moody's to assess sovereign creditworthiness.

### Anticipated rise in social debt is unlikely to affect France's Aaa, at least in the medium term

Moody's notes that the affordability of public debt (defined as the ratio of interest payments to the revenue of the central government) in France is weakening (i.e. the ratio is rising), but remains consistent with a Aaa rating<sup>1</sup> under the most plausible scenarios.

FIGURE 1  
General Government Debt (2008)



Source: Eurostat and CADES

<sup>1</sup> Please refer to Moody's Special Comment entitled [Aaa Sovereign Monitor, March 2010](#).

Although Moody's does not expect France's Aaa sovereign rating to experience pressure in the near term, we note that an unchecked rise in social debt coupled with the absence of an appropriate policy response would result in a further deterioration in France's public debt metrics. It would also suggest that France's debt 'reversibility' (i.e. the ability of the government to repair the balance sheet of the public sector after a shock) is even more limited than currently estimated. This would further reduce France's still substantial, albeit diminishing, 'distance-to-downgrade'.

## French Social Insurance: a highly supportive system

### French social insurance provides compulsory and universal protection

The social insurance system guarantees all French residents the necessary means to ensure decent living conditions for themselves and their families. The SSS is divided into four branches, each providing protection and compensation against hazards linked to (i) health; (ii) workplace accidents and illnesses; (iii) old age and widowhood (pensions); and (iv) family. Protection against unemployment or loss of employment (UIS) is a separate entity apart from the SSS but has been part of the overall French welfare system since 1958. All French residents are obliged to be members of both the SSS and the UIS, and are therefore required to contribute financially to both systems.

The central government is the ultimate decision-maker with regard to the rules governing the SSS and UIS, in that it decides the criteria and processes by which beneficiaries receive payments and the various system entities are financed, in collaboration with employers' representatives and employees' unions.<sup>2</sup>

### Agencies benefit from a high degree of supervision from the state

There are a number of agencies taking part in the organisation, implementation and financing of the French social insurance system. The architecture reflects a series of reforms initiated in 1945, with the aim of involving representatives of both employers and employees in the management of social insurance. There are three large players: the Agence Centrale des Organismes de Sécurité Sociale (ACOSS), the Caisse d'Amortissement de la Dette Sociale (CADES) and Unedic (or Union Nationale pour l'Emploi dans l'Industrie et le Commerce).

- » ACOSS manages cash flows related to the payment of benefits and also has the power to collect social insurance contributions and taxes on behalf of the General Regime<sup>3</sup>. Given its status, ACOSS operates under dual oversight by the Ministry of Economy and Finance and the Ministry of Health. These supervisory authorities appoint ACOSS's executive director, approve every decision of ACOSS's board of directors, have permanent representatives on this board and receive daily reporting on ACOSS's cash position. Every year, as part of the drawing-up of the general social security budget law (for year N+1), the state sets an annual limit (*plafond de ressources non permanentes*) on the amount of short-term debt that ACOSS is allowed to assume. This limit corresponds to the maximum deficit that the General Regime of the SSS is expected to incur during the year N+1.
- » CADES was created by the French government in 1996 with the primary purpose of assuming the accumulated deficits of the General Regime – i.e. ACOSS's short-term debt – by resorting to

<sup>2</sup> Legal arrangements can be found in the Social Security Code and in general social security budget laws

<sup>3</sup> The General Regime applies to salaried employees and assimilated workers, it covers 80% of the population. In addition to this, some specific regimes, such as the regimes for independent and agricultural workers, remain despite an historical consolidation. . Together they form the Social Security System (SSS).

long-term borrowings. In order to redeem this debt while simultaneously covering interest charges and CADES's operating costs, it was endowed with a dedicated tax resource in the form of the CRDS (*Contribution au Remboursement de la Dette Sociale* or Contribution to the Repayment of Social Security Debt). As an EPA, CADES operates under the dual authority of the Ministry of Economy and Finance and the Ministry of Health. In addition to the supervisory responsibilities described above relating to ACOSS, it is worth noting that all transfers of debt to CADES must be agreed by a vote of parliament as part of the rules governing the LFSS. Moreover, CADES's board of directors is responsible for approving its debt issuance programme before being submitted for formal approval by the Ministry of Economy and Finance each year.

- » Unedic is a not-for-profit entity created under France's "1901 association law" in 1958, and is responsible for the management of the UIS. It is jointly managed by the major employers' representatives and unions representing employees in France. Unlike EPAs, Unedic benefits from greater autonomy from the state, which does not exercise a formal administrative oversight (*tutelle*). However, Unedic is subject to a strict code of operation, which stipulates that the rules governing benefits and contributions under the UIS have to be agreed by the state and must result in Unedic enjoying a balanced financial position.

---

### Compulsory contributions levied on salaries form bulk of system resources

The social insurance system's revenues derive from social insurance contributions based on wages (paid by employers and employees) and national taxes (largely levied on wages), of which the key tax is the CSG.<sup>4</sup> According to the French National Institute of Statistics and Economic Studies (INSEE), social insurance contributions for the entire social insurance system (i.e. the UIS and SSS) totalled €304 billion in 2008 (providing 68% of the system's total revenue), while national taxes provided €129 billion (29% of total revenue).

## Accumulating Deficits Are Expected to Lead to Rising "Social Debt" Risk

---

### System has reported persistent deficits over the past two decades

According to a report by the French Audit Board of Social Security (*Commission des comptes de la Sécurité Sociale*), the General Regime has recorded only three annual surpluses<sup>5</sup> over the past two decades (1990-2008). During that time frame, deficits averaged €6 billion annually. Moreover, most recent data indicates that these deficits have widened to approximately €10 billion per year. The UIS has achieved a more balanced performance overall; between 1990 and 2008, its annual deficit averaged approximately €250 million, achieving a balanced position on eight occasions.

The differences between the financial health of the two systems are related less to revenue fluctuations (as both are sensitive to changes in the economic cycle)<sup>6</sup> and more to changes in their expenditure. UIS's expenditure, largely benefits to the unemployed, tends to accelerate during economic downturns and decelerate or even fall during upturns. As a result, its financial position typically improves during times of economic expansion and deteriorates during recessionary periods. Despite the apparent asymmetry, the surpluses generated almost compensate for deficits.

---

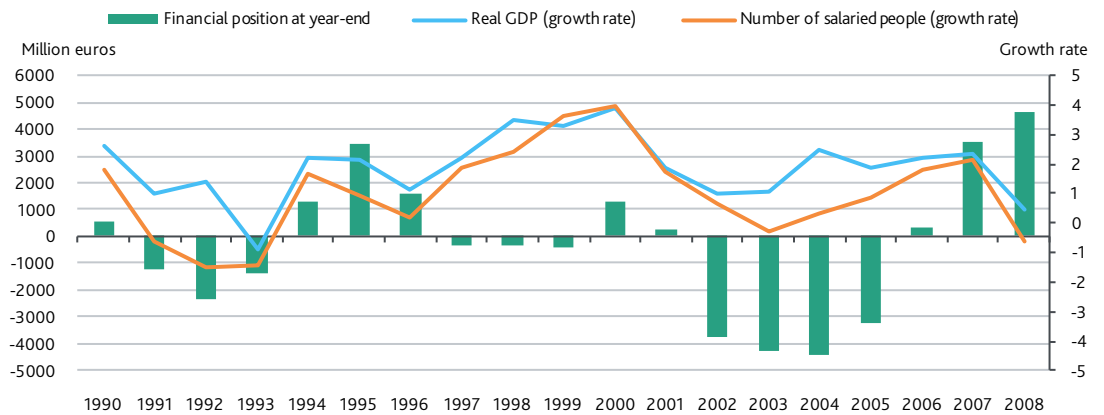
<sup>4</sup> The CSG (*Contribution Sociale Généralisée* or General Social Contribution) is a tax based on the revenue of French residents

<sup>5</sup> Between 1999 and 2001

<sup>6</sup> In both cases, more than 90% of revenues are derived from compulsory contributions principally levied on wages

FIGURE 2

UIS' financial balance

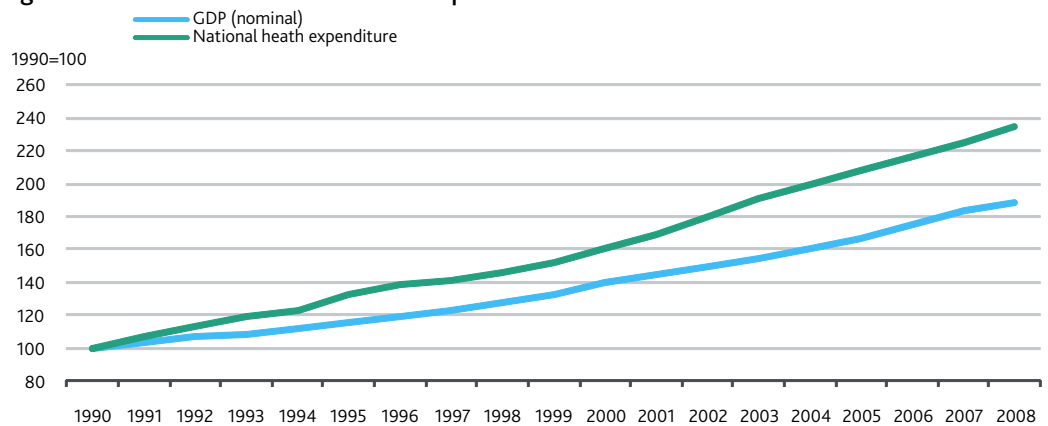


Source: INSEE and Unedic

In the case of the General Regime, deficits largely reflect those accrued in the healthcare sector, as its expenditures, unlike those of the UIS, tend to continue to grow both during periods of economic expansion and contraction, at a rate exceeding that of GDP (see figure 3).

FIGURE 3

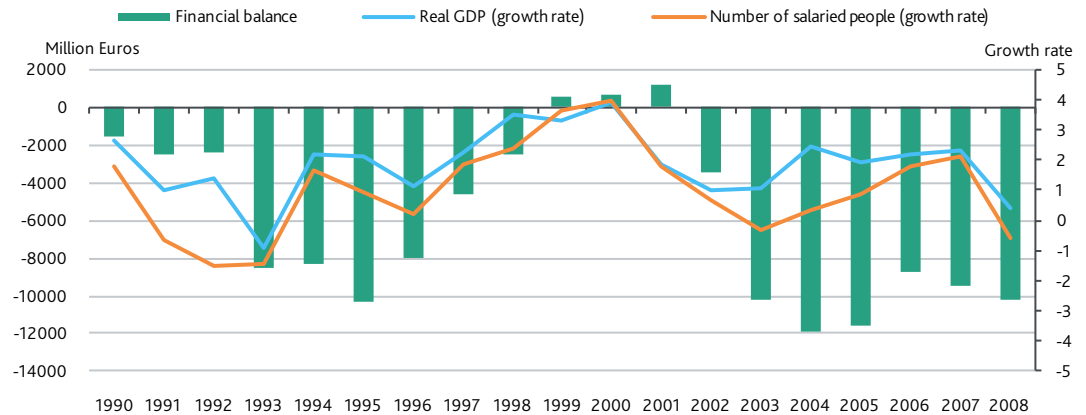
Long-term evolution in GDP and Health expenditure



Source: INSEE and DREES (Direction de la Recherche, des Etudes, de l'Evaluation et des Statistiques)

FIGURE 4

## General Regime's financial position over 1990-2008



Source: INSEE and French Audit Board of Social Security

The General Regime's accumulated deficits are reflected in the growth in CADES's debt since its inception.

### Social insurance debt likely to double from 2008 levels by 2012

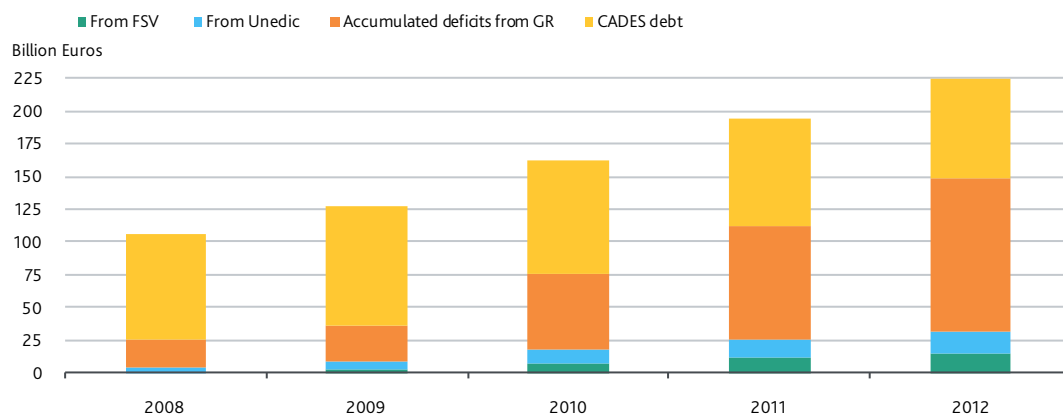
The accumulated debt of all of the agencies in the French social insurance system (i.e. ACOSS, CADES and Unedic) is expected to rise to €224 billion in 2012 from approximately €105 billion in 2008 reflecting persistent and rising deficits.

- » Forecasts for wages and GDP remain negative given economic conditions in France. As a result, the revenues of the main regime of the SSS (General Regime) are expected to fall by an average of 0.9% year-on-year in 2009 and 2010. In turn, ACOSS's annual deficit is expected to reach €23 billion in 2009 and €31 billion in 2010 according to the general social security budget law for 2010. Forecasts are based on prudent assumptions; they anticipate a fall in wages of 2.25% in 2009 and 0.4% in 2010 as well as a 2.2% drop in real GDP during 2009, before improving slightly in 2010 (+0.8%). Moreover, as General Regime's deficit reduction is not linked to the buoyancy of the economy, any recovery from the economic downturn will only serve to stabilise deficits; therefore forecasts beyond 2010 by the central government are based on stabilised deficits at €30 billion annually.
- » In the same way, an unbalanced financial position is anticipated for the FSV (Solidarity's Pension Fund or *Fonds de Solidarité Vieillesse*), whose major revenue source is the CSG. As FSV is not designed to cover deficits, its expected deficits (approximately €4 billion per year) could be either financed through debt transfer to CADES<sup>7</sup>, or supported by ACOSS which is in charge of collecting FSV's revenue.
- » According to most recently published projections (*Equilibre Financier de l'Assurance Chomage* on the financial balance of the UIS), Unedic's financial position is expected to have deteriorated from a surplus of €4.6 billion in 2008 to a deficit of €1.1 billion in 2009 and weaken even further to a deficit of €4.1 billion in 2010.

<sup>7</sup> This option was chosen by the Central Government to deal with FSV's accumulated deficit as of year-end 2008. According to the general social security budget law for 2009, FSV's accumulated deficit as of year-end 2008 was transferred to CADES in the amount of €4 billion.

FIGURE 5

## Social debt estimates



Source: INSEE, Unedic, LFSS for 2010

## Moody's Related Research

### Analysis

- » [Caisse d'Amortissement de la Dette Sociale \(CADES\), September 2008 \(111043\)](#)
- » [Caisse d'Amortissement de la Dette Sociale \(CADES\), May 2010 \(124375\)](#)
- » [Agence Centrale des Organismes de Sécurité Sociale \(ACOSS\), November 2008 \(112868\)](#)
- » [UNEDIC, October 2009 \(119607\)](#)

### Special Comment:

- » [Aaa Sovereign Monitor, March 2010 \(123414\)](#)

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Report Number: 124135

**Author**  
Lucie Villa

**Editors**  
Sébastien Hay  
Matthew Bridle

**Production Associate**  
Judy Yuen

© 2010 Moody's Investors Service, Inc. and/or its licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

**CREDIT RATINGS ARE MOODY'S INVESTORS SERVICE, INC.'S ("MIS") CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES. MIS DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL, FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. CREDIT RATINGS DO NOT CONSTITUTE INVESTMENT OR FINANCIAL ADVICE, AND CREDIT RATINGS ARE NOT RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. CREDIT RATINGS DO NOT COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MIS ISSUES ITS CREDIT RATINGS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.**

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT. All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. Under no circumstances shall MOODY'S have any liability to any person or entity for (a) any loss or damage in whole or in part caused by, resulting from, or relating to, any error (negligent or otherwise) or other circumstance or contingency within or outside the control of MOODY'S or any of its directors, officers, employees or agents in connection with the procurement, collection, compilation, analysis, interpretation, communication, publication or delivery of any such information, or (b) any direct, indirect, special, consequential, compensatory or incidental damages whatsoever (including without limitation, lost profits), even if MOODY'S is advised in advance of the possibility of such damages, resulting from the use of or inability to use, any such information. The ratings, financial reporting analysis, projections, and other observations, if any, constituting part of the information contained herein are, and must be construed solely as, statements of opinion and not statements of fact or recommendations to purchase, sell or hold any securities. Each user of the information contained herein must make its own study and evaluation of each security it may consider purchasing, holding or selling. NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY SUCH RATING OR OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

MIS, a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MIS have, prior to assignment of any rating, agreed to pay to MIS for appraisal and rating services rendered by it fees ranging from \$1,500 to approximately \$2,500,000. MCO and MIS also maintain policies and procedures to address the independence of MIS's ratings and rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold ratings from MIS and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at [www.moody.com](http://www.moody.com) under the heading "Shareholder Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

Any publication into Australia of this Document is by Moody's affiliate Moody's Investors Service Pty Limited ABN 61 003 399 657, which holds Australian Financial Services License no. 336969. This document is intended to be provided only to wholesale clients (within the meaning of section 761G of the Corporations Act 2001). By continuing to access this Document from within Australia, you represent to Moody's and its affiliates that you are, or are accessing the Document as a representative of, a wholesale client and that neither you nor the entity you represent will directly or indirectly disseminate this Document or its contents to retail clients (within the meaning of section 761G of the Corporations Act 2001).