

## Parental Insurance and Childcare Statements and Comments

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### Part I: PUBLIC CHILDCARE

#### 1. Background on Public Childcare in Latvia

##### a. Legislation

Pre-schools in Latvia are regulated by the 'Law on Education' (1999), the 'Law on General Education' (1999), and the 'Law on Municipalities' (1994).<sup>1</sup> The law guarantees a right to childcare for all children of citizens, permanent residents of Latvia, as well as for EU citizens with residence permit. Some important amendments in the Law on Education were passed in 1999, which made pre-school education mandatory for children aged 5-6 years. On the state level, public pre-schools are overseen by the Ministry of Education and Science.

Today, local governments are almost fully responsible for the provision of public childcare.<sup>2</sup> Although a large share of costs is borne by local governments' budgets, parents have to pay for the meals and the central government pays for pre-school education of children aged 5-6 years.<sup>3</sup> However, the central government sets out certain minimum quality standards with respect to minimum cost per child, group size, and teacher training. The minimum costs per child are set at the level of 640 Ls per year, of which 340 Ls must be for teachers' salaries. For children aged 5-6 years the minimum per child annual cost is 902.5 Ls. The minimum/maximum group sizes in public pre-schools are 10-12 for children aged 0-3 years; 10-16 for children aged 3-4 years; and 12-20 or 8-16 for children aged 5-6 for cities (and regional centres) or other places, respectively. Although the ratio of children to staff (teachers) is not regulated, the ministry's recommendation is the 10 to 1 ratio. From September 1<sup>st</sup>, 2004 there will be a requirement for all pre-school teachers to have a university degree with specialisation in pre-school education, or to be enrolled in such an academic program.

The law also permits the operation of private pre-schools, which are mostly financed by parents' fees. Sizes of fees are not regulated by the state.<sup>4</sup> However, private pre-schools must also meet the minimum quality standards set by the state, with the exception of minimum group sizes.

##### b. Childcare and Women's Employment: Some Facts

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<sup>1</sup> There are also regulations set by the Cabinet of Ministers and the Ministry of Education and Science.

<sup>2</sup> Before 1997 salaries of public preschools' staff were paid from the central government budget. This responsibility was also transferred to the local governments with major change in the Law on Municipalities that took place in 1997.

<sup>3</sup> However, local governments may choose to exempt groups such as very poor families and single mothers from paying the fees.

<sup>4</sup> Local governments may choose to pay some of the costs of the private preschools, as is the case, for example, in Riga and Jelgava.

Compared to the EU average, employment rates of women in Latvia have been relatively high and rising (see Table 2 in the Appendix). However, for the year 2002 a woman's chance of being employed was about seven percent less than that of a man, and the difference was much larger for women aged 20 to 34 years old (see Table 3 in the appendix). This suggests two things. First, a Latvian household is characterised by the dual-earner model, where both male and female are likely to be working. Second, it is probably not a dual-carer model since women seem to be more likely to be involved in raising children.<sup>5</sup>

As one of the aims of the Soviet-style central planning was attracting more women to work, Latvia inherited an extensive system of public childcare. Unfortunately, due to the worsening demographic situation and deterioration of public finances many public pre-schools had to be closed. As shown in Table 4, the number of pre-schools in 2002 was less than half of what it was in 1990. Over the last several years, however, the proportion of children in pre-schools has been increasing and in the year 2002 it was 51.6 percent. This proportion is very low for children aged 0-1 years and rather high for children aged 5-6 years (see Table 4 in the appendix). The number of private pre-schools has increased from 12 in 1999 to 22 in 2003. However, the proportion of children enrolled in private pre-schools is still tiny. In 2003 it was only about 2 percent of the total number of children enrolled in pre-schools.

Low enrolment rates most likely reflect excess demand, rather than the lack of it. Average capacity utilisation of public pre-schools is at 122 percent, two year long queues are commonplace, and it is considered wise to apply for a place in pre-school well before a child is born.<sup>6</sup>

Do public pre-schools in Latvia deliver high quality care? It's hard to tell, of course, but one sure thing is that the pre-schools are severely under-funded. The Secretariat of the Minister for Special Assignments for Children and Family Affairs has just finished collecting data from the local governments about pre-school institutions. Some of the results are summarized in Table 5. It appears that the perceived lack of funds reported by the local governments, on average, amounts to almost a third of current financing. Although the local governments and the pre-schools are probably doing their best, the fact that the pre-schools are literally overfull with children is also likely to impair the quality of childcare. Also, there is much regional variation in accessibility of public childcare, costs per child, and lack of funds. It seems that the major reason for this variation is that local governments in economically depressed areas cannot raise enough money.

### c. Policy Context

Family-oriented policies were one of the top priorities of the previous and the present governments, as exemplified by the establishment of the new post of the Special Tasks Minister on the Issues of Children and Families. The minister's secretariat developed the 'Concept of benefits for families with children', a policy spanning the next 10-20 years. The aim of this policy is to build a healthy and favourable social and economic environment for family development. Stimulation of availability of pre-schools, improving the quality of childcare, and facilitation of variety of pre-schools are among the tasks identified in the concept.

<sup>5</sup> Of course, the fact that women's particularly low labour market activity coincides with being of child-bearing age may have other explanations, but it is also consistent with our suggestion.

<sup>6</sup> Capacity utilisation is defined as the ratio of accommodation capacity to enrolment. Simple average across regions was calculated.

## 2. Relevance and transferability

The proposed policy is in accordance with the policy priorities of the Latvian government, as laid out in the National Employment Plan, such as achieving gender equality and lifelong learning. There is substantial empirical evidence that reduced childcare costs are associated with greater employment of married women and other household members.<sup>7</sup> However, subsidisation of childcare may also have adverse effects on employment. As first noted by Heckman (1974), additional subsidies may lead to fewer hours of work just as higher wages can induce fewer hours for those already working.<sup>8</sup> Gustafsson and Stafford (1992) cite Hoem *et al* (1990) as arguing that the generosity of the Swedish child care system explains a part of the growth in both participation rates and part-time work of Swedish women. Even so, as the average income level in Latvia is very low as compared with Sweden, these adverse effects are likely to be very small.

The extent of childcare subsidies as such, however, is unlikely to be an issue in Latvia - at least solely from the point of view of promoting women's employment. Latvia has inherited a tradition of universal public provision of childcare at little more than zero cost to its users. Thus, it is poor accessibility of pre-schools that is likely to be the main impediment to women's employment, not the price of (public) childcare. In our view, the biggest potential is in learning more about how public pre-schools are financed by the central government, local governments, and private households. In particular, the Latvian government should definitely take note of the practice to tie parents' fees to their incomes and employment status. It should be recognised, however, that public provision of childcare is a multi-faceted issue, which transcends its effects on women's employment.<sup>9</sup>

However, there is definitely much to learn from how the Swedish pre-schools are run. Having visited a preschool in Stockholm during the Peer Review meeting, my observation is that the quality of childcare is much higher than it is in Latvia. Somehow, it seems that there is much 'bottom-up' innovation and diversity in the Swedish childcare model. I would therefore label Swedish approach to childcare as 'proactive', in which the staff is very involved in fostering children's development. In contrast, Latvian approach to childcare can be described as 'passive', *ie* being a bit more than organized 'child minding'. Since there is a widespread belief that child development is positively associated with childcare quality, transferring the Swedish model is highly desirable. However, whether it is *transferable* depends on what explains the performance of Swedish preschools. For example, if quality mostly depends on spending per child and a host of cultural factors, transferability is questionable. Unfortunately, at this stage I may only advance a very tentative explanation of the preschool quality in Sweden. First, I believe one has to go deeper than simply looking at aggregate indicators such as staff-child ratios.<sup>10</sup> Second, some of the vital ingredients of the 'Swedish formula' seem to be extensive freedom for 'childcare professionals to run things their way', competition among preschools,

<sup>7</sup> See, among others, Blau and Robins (1988) and Kimmel (1998) for studies using U.S. data and Gustafsson and Stafford (1992) for a study using Swedish data. The findings for single mothers are typically less robust.

<sup>8</sup> In other words, the income effect may be substantial.

<sup>9</sup> Further thinking along these lines indicates that we must also consider competition effects and aspects of public finances with multiple levels of government.

<sup>10</sup> Inputs into childcare quality such as group size, staff-child ratio, and provider training are easily observable and often serve as a basis for quality comparisons. However, a provocative study by Blau (1999) found that these childcare inputs experienced during the first three years of life had little impact on child development outcomes in the United States, as measured by a battery of developmental tests.

relatively easy entry into the 'preschool business', and above-average salaries of the teachers. I think that a comprehensive study involving childcare professionals in Latvia is definitely a must here.

### 3. The issues

At this moment there is a lively discussion about the provision of public childcare in Latvia, both in the legislature and the media. The whole debate revolves around the severe lack of places in public pre-schools and is really about ways to deal with it. One obvious solution is for local governments to build more pre-schools and accommodate the demand at the present subsidised price. That solution is also likely to raise women's employment, just like it did in Sweden. However, more pre-schools means higher taxes, or less spending on other public needs.<sup>11</sup> Also, an increase in public provision at current (very low) prices will drive out private suppliers, killing competition.<sup>12</sup>

A possible solution is to raise fees to a level where excess demand is eliminated. That will eliminate the inefficiencies of non-market rationing, such as incentives to bribe public officials. A more elaborate system of financing would also be needed to ensure entry of private providers who could compete with public pre-schools on equal terms. The role of the central government should largely be confined to that of fiscal equalisation between regions.

## Part II: PARENTAL LEAVE

### 1. Background on parental leave in Latvia

According to the law, each employed woman in Latvia has a right to a 112 days long maternity leave, with monthly allowance equal to 100 percent of her average earnings.<sup>13</sup> A man has a right to a ten day long paternity leave with 80% replacement rate. These leave entitlements are exclusive for mothers and fathers. The allowances are financed from the social payroll taxes. They are exempt from personal income and payroll taxes and there is no ceiling on their size. In addition to maternity/paternity leaves, both mothers and fathers have a right to unpaid parental leave to care for a child that is less than 8 years old.<sup>14</sup> An employee -also has a right to a reduced workload to care for a child who is less than 14 years old.

I now turn to the data to evaluate the extent to which parental leave is used by men and women. Given the generous allowance, it is very likely that maternity leave is used by all mothers. Based on results of the Labour Force Survey (LFS), our estimate is that 14,362 women took unpaid parental leave in 2002, compared to only 362 men. There is also some evidence of a

<sup>11</sup> Being largely unable to pay for the increased provision, local governments call on the national government to step in with funding for more preschools. In general, provision of services such as public childcare should ultimately be up to the local governments, as they are 'closer to the people'. The national government's role in this respect should be confined to fiscal equalisation, *ie* helping poor regions deliver certain minimum standards of provision.

<sup>12</sup> One alternative solution offered by some of the local governments is to offer a modest subsidy for parents who decide to put their children in a private preschool. This proposition may not be justified on equity grounds since it will largely be a transfer to the high income families, who are able to afford a private preschool.

<sup>13</sup> The average is taken over the two previous months. There is an additional 14 days leave in case of complications during pregnancy.

<sup>14</sup> Beneficiaries receive a modest monthly allowance (30 Ls) from the Government.

serious conflict between childcare demands and work. According to the LFS, 5.5 percent of all non-employed women said the reason for leaving their last job was 'childcare', as compared to only 0.4 percent of all non-employed men who said so.

Recent policy initiatives have focused on increasing the size of childbirth benefit (which was recently tripled) and family state benefits. Earlier this year the Ministry of Welfare drafted the 'Concept of benefits for families with children', which highlighted the need to stimulate both parents to take leave after childbirth, and facilitate re-entering the labour force after maternity leave.

## 2. Relevance and transferability

As described earlier, a woman in Latvia has the right to a 16 week long maternal leave with full pay, which can later be extended to another 1.5 years of unpaid leave with her workplace preserved. Therefore, as compared with Sweden:

- a) the parental leave in Latvia is shorter; and
- b) fathers cannot take it.<sup>15</sup>

We discuss transferability of these two aspects.

Should parental leaves be longer? That is not an easy question to answer. Critics argue that parental leave mandates reduce economic efficiency and have a particularly adverse impact on women, in terms of both their wages and their prospects for career advancement. That concern was also expressed by the Swedish expert. Supporters of parental leave argue that the entitlements improve the health and well-being of children, which might not occur if the benefits of leave represent externalities which are not adequately valued by agents negotiating labour contracts. Another powerful argument is that under asymmetric information in the market, adverse selection arises, *ie* a company voluntarily offering leave is likely to attract a disproportionate number of 'high' risk employees (Summers, 1989). Do the benefits of longer leave outweigh the costs of it? A study by Ruhm (1998) provides some interesting evidence in this regard.<sup>16</sup> Ruhm (1998, p. 315) finds that 'parental leave guarantees raise the employment of women, but, at longer durations, may be paid for through the receipt of lower relative wages.' This point is illustrated in Table 1, adapted from Ruhm, which shows the predicted impact of specified paid leave entitlements, as compared with the case of no mandatory leave. Therefore, if Latvia were to double its parental leave entitlement from 16 to 32 weeks, the model's prediction would be that this would reduce women's relative wage and probably leave the employment to population ratio unaffected. Apart from that, doubling of duration of parental leave is likely to double the policy's current cost to the budget.

<sup>15</sup> Fathers can take the 1.5 years unpaid leave as well. However, the maternity leave is exclusively for women.

<sup>16</sup> The study investigates the economic consequences of rights to paid parental leave in nine European countries (including Sweden) over the 1969 through 1993 period.

Table 1: Predicted effect of paid leave entitlements on the difference between female and male outcomes, versus no leave

Leave duration (full pay weeks)	Employment to population ratio <sup>17</sup>	Hourly wages
8 weeks	3.4%	-0.9%
16 weeks	4.3%	-2.1%
24 weeks	4.5%	-3.0%
32 weeks	4.0%	-3.4%

*Source: This Table is an adaptation of Table VI, columns (a) in Ruhm (1998, p.308), adjusted for full pay weeks. The percentages are estimated differentials between female and male labour market outcomes versus no leave.*

This prediction seems intuitively plausible. Brief periods of leave probably impose few costs on the employers. However, extended work absences may impose substantial non-wage costs on the firm. There is also the depreciation of human capital associated with prolonged absence from work. Of course, one may doubt the accuracy of Ruhm's findings and their applicability to Latvia.<sup>18</sup> However, we think that in the absence of more definitive empirical evidence one has to be cautious about further extending duration of parental leave in Latvia.

On the other hand, introducing 'fathers-only' parental leave (or increasing paternity leaves) may stimulate greater fathers' involvement with childcare, which is definitely lacking in Latvia. Paternity leaves may complement maternity leaves to ensure a smooth transition until a child is old enough to be eligible for a pre-school. True, increase in the duration of paternity leaves is likely to increase the costs to the budget. In order to minimise budgetary pressure, it could be worthwhile re-evaluating the size of the allowance (as a percentage of the wage) and also introduce limits on the maximum size of the allowance.

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<sup>17</sup> Note that some of the increase in employment to population ratio is 'illusory', as it merely comes as a result of reclassification of those on parental leave as 'employed but absent from work', rather than 'not employed'. Ruhm estimates this effect to lie between one quarter and one half of the total differential.

<sup>18</sup> For one thing, Latvia was not among the countries in Ruhm's sample, which makes predictions for it less accurate. Second, the data on wages used in estimation are mostly for the manufacturing sector, which casts some doubts on accuracy of the findings with respect to wages.

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#### Persons Interviewed

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## Appendix

Table 2: Key Labour Market Indicators: Latvia vs. the EU (age 15-64)

Indicator	Latvia	EU average		Latvia
	2001	2001	2002	2002
Activity rate, men	72.8	78.4	78.4	73.9
Activity rate, women	62.1	60.3	61.0	64.1
Employment rate, men	61.8	73.3	72.9	64.3
Employment rate, women	56.1	55.1	55.6	57.0
Unemployment rate, men	14.7	6.5	7.1	13.1
Unemployment rate, women	12.1	8.6	8.9	11.0

Source: Central Statistical Bureau of Latvia and OECD.

Table 3: Activity and employment rates by gender and age: Latvia and EU-15, 2002

	Activity rates		Employment rates	
	Latvia	EU-15	Latvia	EU-15
Men, 15-19	18.8	30.9	13.6	26.1
Women, 15-19	11.5	25.9	6.5	21.7
Men, 20-24	73.2	68.9	61.8	59.1
Women, 20-24	58.8	59.1	47.2	50.3
Men, 25-34	92.1	91.6	81.6	84.6
Women, 25-34	77.2	74.8	69.1	67.3
Men, 35-44	89.0	94.6	76.6	89.4
Women, 35-44	85.2	74.9	76.3	67.3
Men, 45-54	86.2	90.4	76.2	85.7
Women, 45-54	84.3	69.2	77.4	64.7
Men, 55-64	57.2	54.1	50.8	50.8
Women, 55-64	38.7	33.4	35.6	31.2

Source: Calculation based on LFS data for Latvia; OECD for EU-15.

Table 4: Number of pre-schools and proportion of children enrolled

Year	Number of preschools	Enrolment in public pre-schools, number of children	Number of children aged 0-6 years old	Proportion of children enrolled in pre-schools, percent
1980	926	113,737	n/a	n/a
1985	993	131,074	n/a	n/a
1990	1,123	111,471	n/a	n/a
1995	608	72,847	n/a	n/a
2000	561	61,759	139,762	44.2%
2001	552	61,451	135,198	45.5%
2002	551	69,194	134,205	51.6%

Source: Central Statistical Bureau of Latvia, Bulletin on Education Institutions in Latvia 2002-2003

Table 5: Provision of childcare in Latvian regions

	Mean	Standard Deviation	Minimum	Maximum
Proportion of children in pre-schools	52.4%	15.1%	40.6%	78.8%
Number of children per staff member	8	1	7	10
Current annual costs per child, LVL	644	65	538	691
Perceived lack of funds as percentage of current financing	30.9%	26.4%	0.0%	66.2%

Source: Secretariat of the Special Tasks Minister on the Issues of Children and Families

Table 6: Number of children in pre-schools by age group in 2002

Age group	Number of children in pre-schools	Number of children	Proportion of children in pre- schools, percent
1 year	1,407	20,042	7.0%
2 years	7,962	19,050	41.8%
3 years	12,149	17,968	67.6%
4 years	11,972	18,361	65.2%
5 years	16,576	19,192	86.4%
6 years	17,308	20,944	82.6%

Source: Central Statistical Bureau of Latvia, Demographic Yearbook 2000-2003, Bulletin on Education Institutions in Latvia 2002-2003