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Measuring Regional Economic Opportunities: A New Approach Through the Regional Economic Opportunities Index and the Regional Deficit Coefficient

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FISCAL AND DISTRIBUTIONAL EFFECTS OF THE CHANGE IN THE SOCIAL SECURITY MODEL FOR CIVIL SERVANTS IN BULGARIA

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Abstract: This study analyses the fiscal and distributional effects of the phased introduction of personal social insurance contributions for civil servants under the Civil Servants Act (CSA) and for employees under the Judiciary Act (JA). The main argument is that the regulatory change should not be assessed through the formal transfer of part of the social insurance contribution to the employee, but rather through the actual economic incidence and the net effect on the consolidated public sector. When net income is preserved through an increase in gross remuneration, a gross-up effect on wages arises, which limits the immediate fiscal savings and changes the distribution of flows among the state budget, the State Social Insurance system, the National Health Insurance Fund (NHIF), universal pensions funds (UPF), and households. Three scenarios are considered: no compensation; full compensation of net income; and compensation within a constrained personnel budget. The analysis shows that the first scenario produces the clearest direct budgetary effect, but through a reduction in employees' disposable income, whereas under full compensation the reform is primarily of an institutional and distributional character. Over the medium term, the fiscal outcome depends on the rules governing remuneration indexation, staff numbers, the maximum insurable income, and the manner in which the technical compensation is incorporated into the future wage base.

Keywords: civil servants, social insurance contributions, budget effect, public finance, distributional effects, SSI, NHIF, UPF.
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1. Introduction

The social insurance regime for civil servants in Bulgaria has traditionally differed from that applicable to persons under employment contracts in terms of how the mandatory social insurance burden is distributed. Until mid-2026, social insurance contributions for civil servants were borne by the state budget through the respective public employer. Amendments to the Social Insurance Code (SIC) and the Health Insurance Act (HIA) introduce a sharing of the contribution burden between the social insurance contributor and the insured person (SIC, Article 6, paragraph 5a; HIA, § 20).

Parallel to the amendment, compensation of remuneration is provided for, so that the net income received is maintained through an increase in gross remuneration (Ministry of Finance, 2026b).

This arrangement transforms the reform from a purely regulatory change into a public finance issue. The statutory designation of the payer does not, in itself, determine who bears the economic burden. When the budgetary employer increases gross remuneration in order to maintain net income, part of the new employee social insurance contribution is financed by the budget itself. Therefore, the analysis should distinguish three aspects: legal incidence, economic incidence, and the consolidated fiscal outcome.

The aim of the article is to analyse and assess the fiscal and distributional effects of the change in the social insurance model for civil servants. To achieve this aim, the following research tasks are set: to clarify the mechanism of tax and social insurance incidence; to trace financial flows across institutional sectors; to model three compensation regimes; to analyse the distributional consequences across income groups; and to assess the medium-term sustainability of the Personnel Fund.

2. Theoretical, Institutional, and Regulatory Framework

Theoretical framework. The economic interpretation of the reform fits naturally within the classical public finance framework developed by Richard

A. Musgrave (1959). The distinction between the allocation, distribution, and stabilization functions is particularly useful here, as the measure under consideration directly affects disposable income, public expenditure, and the allocation of resources among current consumption, social insurance, and pensions accumulation.

This approach is particularly useful here because it demonstrates that a single reform can be nearly neutral for the consolidated balance while simultaneously producing significant distributional consequences. Shifting a payment from a budgetary employer to an employee does not necessarily constitute a resource saving if salaries are increased in parallel. It may instead represent a change in the institutional routing of the same publicly funded flow.

The theory of tax incidence, developed also by Joseph E. Stiglitz and Jay K. Rosengard (2015), requires an important distinction: the legal obligation to pay a tax or social insurance contribution does not necessarily indicate who bears the ultimate economic burden. This burden may be reflected in lower remuneration, higher prices, or lower returns. In the case of labour-related social insurance contributions, this means that the formal "employer : employee" ratio is not a sufficient measure of the actual distribution of the burden.

For the Bulgarian public sector, the institutional specifics lies in the fact that both the employer and the recipients of a large portion of social insurance revenue belong to the General Government sector. When a state employer increases gross remuneration from which a personal contribution for the State Social Insurance system (SSI) or the National Health Insurance Fund (NHIF) is withheld, part of the operation constitutes an intra-sectoral flow within the public sector. This does not imply that the operation is economically irrelevant: it affects the budgets of individual subsectors and the rights of the insured persons. However, it should not be double-counted as an expenditure and, at the same time, as an independent "new" fiscal gain.

This framework should also incorporate the economics of social insurance. Nicholas Barr (2001) considers pensions and insurance systems as mechanisms for risk redistribution, consumption smoothing over time, and responses to uncertainty and incomplete information. This is directly relevant to flows to universal pensions funds: for the budget, they represent a current cash outflow, whereas for the household, they constitute the accumulation of an individual financial asset.

Therefore, the assessment of the reform requires the simultaneous application of three criteria: fiscal efficiency, horizontal equity, and intertemporal distribution. Fiscal efficiency demands that the real cost of compensation be accounted for. Horizontal equity implies that individuals with similar incomes and comparable social insurance rights should be subject to a comparable structure of the social insurance burden. The criterion of intertemporal

distribution requires recognition that part of today's budgetary expenditure on universal pensions funds is transformed into future pensions assets for the insured person.

Institutional and Regulatory Framework. Pursuant to Article 6, paragraph 5a of the Social Insurance Code (SIC), the change applies to civil servants under the Civil Servants Act and to the categories of persons under the Judiciary Act specified in Article 4, paragraph 1, items 2, 3 and 10 of the SIC. For the period from 1 August to 31 December 2026, contributions are distributed between the social insurance contributor and the insured person at a ratio of 80:20, while from 1 January 2027, the second stage begins, with a 60:40 distribution for the General Sickness and Maternity Fund and the Unemployment Fund taken together (SIC, Article 6, paragraph 5a; NSSI, 2026a).

For the first stage, persons born after 31 December 1959 and insured through UPFs make contributions to three funds, the total amount being distributed between the social insurance contributor and the insured person as follows: for the Pensions Fund, a total contribution of 14.8%, distributed at 11.8% and 3.0%; for the General Sickness and Maternity Fund, a total contribution of 3.5%, distributed at 2.8% and 0.7%; and for the Unemployment Fund, a total contribution of 1.0%, distributed at 0.8% and 0.2%. From 1 January 2027, the contribution to the Pensions Fund for the same group is distributed as 8.22% paid by the social insurance contributor and 6.58% paid by the insured person; for persons born before 1 January 1960, the respective amounts are 11.02% and 8.78% (SIC, Article 6, paragraph 5a, items 1–2; NSSI, 2026a).

From 1 August 2026, the maximum monthly insurable income increases from EUR 2,111.64 to EUR 2,300. The measure forms part of the parameters of the State Public Social Insurance Budget Act for 2026 (State Public Social Insurance Budget Act for 2026; NSSI, 2026a).

According to official information from the NSSI, the insurable income of civil servants includes received or accrued gross monthly remunerations, capped at the maximum insurable income. The scope of the change should not be equated with all persons included in total budgetary personnel expenditure. Military personnel and certain categories of civil servants under special laws are subject to a different social insurance regime; the NSSI separately presents the individuals under Article 4, Paragraph 1, Item 4 of the Social Insurance Code and the specific provisions (NSSI, 2026b; NSSI, 2026c). The main parameters of the change are summarized in Table 1.

Table 1

Main parameters of the social insurance reform

Parameter	01.08–31.12.2026	Since 01.01.2027
Contributor : insured person ratio	80 : 20	60 : 40
Pensions Fund – persons born after 31.12.1959, insured through UPFs	11.8% / 3.0%	8.22% / 6.58%
General Sickness and Maternity Fund	2.8% / 0.7%	60 : 40 jointly with the Unemployment Fund
Unemployment Fund	0.8% / 0.2%	60 : 40 jointly with the General Sickness and Maternity Fund
Health insurance	80 : 20 of the total rate	60 : 40 of the total rate
Maximum monthly insurable income	EUR 2,300	Pursuant to the State Public Social Insurance Budget Act for 2027
Compensation	Provided for to maintain net income	Depends on remuneration policy

Source: Authors' compilation based on the SIC (Art. 6, para 5a), the HIA (§ 20), and the NSSI (2026a).

2. Data, scope, methodology, and scenario analysis

The quantitative analysis uses official administrative and budgetary sources, while acknowledging the limitation that there is no publicly available unified microdata database on the remuneration of all specifically affected individuals. Therefore, the results are presented as scenario-based estimates rather than as a definitive accounting assessment of the budget.

The Integrated Information System of the State Administration (IISDA) publishes annual reports on the baseline staff numbers and vacant positions as of 31 December 2025, with the data populated and approved by the respective administrations. While these sources are suitable for determining the scale of

the state administration, they cannot, on their own, identify all persons transitioning to the new social insurance regime (IISDA, 2026a; IISDA, 2026b).

The study uses a baseline of approximately 48,403 authorized positions and 26,073 persons employed under employment contracts in administrative positions. These values are not applied as a direct multiplier for the fiscal effect, but rather as an indication of scale. The rationale is that a portion of the administrative staff is employed under employment contracts and already pays personal contributions, while persons under the Judiciary Act are not fully covered by the IISSA (IISSA, 2026a; IISSA, 2026b).

Methodologically, net remuneration is viewed as a result of gross remuneration, employee social insurance contributions, and income tax. When the policy aims to preserve net income, simply adding the amount of the employee contribution to the gross remuneration is not sufficient. The very increase in gross remuneration itself generates additional social insurance and tax liabilities; that is, a gross-up effect on wages arises (Personal Income Tax Act, Article 42).

The analysis considers three scenarios. In Scenario A, there is no compensation. In Scenario B, net income is fully compensated. Scenario C allows for compensation, but within a restricted general Personnel Fund. The option is necessary because the 2026 budget framework simultaneously imposes constraints on personnel expenditure for some budgetary organizations.

Scenario A – no compensation. The employee's share of the contributions is withheld from the existing gross remuneration. Thus, current budgetary expenditure for employer social insurance contributions decreases without any remuneration increase, while the disposable income of the affected employees falls. Economically, this is equivalent to a reduction in labour compensation.

Scenario B – full compensation. The gross remuneration is increased to a level where net income is preserved. Here, the wage gross-up absorbs a significant portion of the immediate savings from the lower employer contribution. While the higher social insurance base may increase revenues into public funds, these inflows are the result of additional public expenditure.

Scenario C – compensation within a restricted general Personnel Fund. Net income is preserved, but the technical compensation is financed within an already restricted resource—for example, through vacant positions, lower future indexation, bonus restrictions, or headcount reductions. If a positive fiscal effect arises, it stems from the accompanying personnel policy rather than from the transfer of the social insurance contribution share itself.

According to Musgrave's functional framework (1959), the third scenario combines a distributional change with an allocation choice within the public sector: the state redirects a restricted resource from future growth in

remuneration or headcount numbers toward financing the technical compensation. Therefore, its fiscal effect should be interpreted as the result of a package of measures rather than a standalone effect of the social insurance reform. The comparison of the three scenarios is presented in Table 2.

Table 2

Summary of the three scenarios

Indicator	Scenario A No Compensation	Scenario B Full Compensation	Scenario C Compensation within a Restricted Personnel Fund
Employee's net income	Decreases	Preserved	Preserved currently; potential lower future growth
Gross remuneration expenditure	No change	Increases	Increases technically, but is compensated internally
Employer social insurance contributions	Decrease	Gross-up partially neutralizes the effect	Depends on restructuring
SSI/NHIF revenues	Similar under the same base	May increase with a higher base	May increase with a higher base, but with no increase in total resource
Flows to UPFs	Change of payer	Potential growth due to gross-up	Same, but within a restricted fund
Consolidated effect	Positive	Limited/close to neutral	Positive only if other expenditures are actually constrained

Source: Authors' compilation.

1. Effects, Risks, Assessment, and Recommendations

Fiscal Effects. The assessment should distinguish at least four monetary flows: expenditure on gross remuneration; employer social insurance contributions; employee social insurance contributions; and income tax. In addition, the flows directed toward the SSI and the NHIF must be isolated from those toward the UPF, as the latter leave the consolidated public sector and are capitalized in individual accounts.

If there is no compensation, gross remuneration remains unchanged. The employer's share of the contribution decreases, while the employee's share is withheld from the existing remuneration. With an unaltered insurable base, this does not, in itself, increase the revenue of the SSI and the NHIF; it primarily shifts who formally and economically bears the burden. In this case, the budgetary savings have a direct counterpart - lower net income for the employee.

Under full compensation, the mechanism is different. Gross remuneration increases, which, up to the maximum insurable income, generates additional employer and employee social insurance contributions, as well as a higher income tax. A portion of the additional gross expenditure flows back into the public funds, but this does not automatically imply a net fiscal gain, because the revenue itself is generated by higher public spending.

For income above EUR 2,300, the marginal cost of compensation decreases because additional income above the maximum insurable income does not generate new social insurance contributions. This constitutes a significant distributional mechanism: as a percentage of gross income, the social insurance burden is lower for higher remuneration, while employees below the ceiling are fully subject to the proportional contribution rates.

The flow to the UPF requires separate treatment. When the state increases gross remuneration to preserve net income, the portion of the compensation converted into a UPF contribution leaves the general government sector. For the household, however, this same flow forms a financial asset. Consequently, the cash-based fiscal assessment and the welfare assessment cannot be reduced to a single indicator.

Distributional effects. The first distributional effect is between the state budget and households. Without compensation, the burden is shifted to the employee. Under full compensation, the immediate burden remains with the public employer, although the deduction is formally visible on the employee's payslip. This is a typical example of a divergence between legal and economic incidence.

The second effect is between public funds. The SSI and the NHIF may report higher revenue if the gross-up increases the insurable base. For the consolidated budget, these revenues should be assessed against the expenditure that generates them; otherwise, there is a risk of double counting.

The third effect is between the first and second pensions pillars. For individuals insured through UPFs, a portion of the resources is directed toward an individual account. According to Barr (2001), this can be viewed as a mechanism for consumption smoothing over time and managing the risks of old age; however, from the perspective of the current budget, the resource leaves the public sector.

The fourth effect is across income groups. The maximum insurable income caps the absolute amount of employee social insurance contributions for higher salaries. Below the ceiling, the burden varies proportionally, while above it, the average effective social insurance contribution rate decreases. Therefore, the reform has a regressive element when the social insurance burden is assessed as a share of gross income. In the short term, full compensation neutralizes this effect on net income, but not on the budgetary cost of compensation.

Quantitative illustrations. The quantitative examples are illustrative and should not be interpreted as an official budget forecast. If a hypothetical employee has a gross monthly remuneration of EUR 1,500, which is entirely below the maximum insurable income, any technical compensation increases not only the gross remuneration but also some of the related social insurance and tax payments. Therefore, the required wage gross-up is higher than the nominal amount of the new employee contribution.

If gross remuneration is EUR 3,000, social insurance contributions are capped at EUR 2,300. The additional increase above the ceiling generates primarily income tax. Therefore, the required compensation as a percentage of the initial gross remuneration is lower than for income entirely below the ceiling.

The illustration at the aggregate level demonstrates the sensitivity of the result. With 40,000 affected persons and an average insurable income of EUR 1,500 per month, the monthly insurable base is EUR 60 million. An employee social insurance contribution burden of 6–7 percentage points would imply EUR 3.6–4.2 million in monthly employee contributions before compensation and prior to their exact allocation across funds. With 50,000 persons and an average insurable income of EUR 1,800, the base reaches EUR 90 million, and the same range yields EUR 5.4–6.3 million.

For the period August–December 2026, the effect spans only five months. Starting from 2027, the transition to the 60:40 ratio increases the employee's share and the potential cost of the compensation. Consequently, the results for 2026 must not be linearly extrapolated into 2027.

Effect on the Personnel Fund and the Medium-Term Budget. The medium-term outcome depends to a significant extent on how the technical compensation is treated. If it is permanently incorporated into the basic salary and future indexation is applied to the already increased base, the initial gross-up begins to generate a cumulating expenditure. Thus, a one-off technical adjustment becomes a permanent component of the base for future increases.

Under a pre-restricted Personnel Fund, the picture is different. The compensation may displace other future increases. Current net income remains unchanged, but the remuneration trajectory may turn out to be lower than a counterfactual scenario without the reform. Critical to the scientific assessment

is the correct identification of the source of savings: the effect of lower indexation or headcount numbers must not be attributed entirely to the social security reform itself, but should be established through comparison with the trajectory of personnel expenditures in the absence of the reform.

Effects on Incentives and the Labour Market. Greater harmonization of the structures of gross and net remuneration facilitates comparison between civil service positions and regular employment contracts. This reduces part of the information asymmetry in assessing remuneration and the total cost of labour and is relevant to horizontal equity.

Under full short-term compensation, no strong immediate response in labour supply is expected, as net income is preserved. In the medium term, it matters whether the compensation becomes part of the future base and whether subsequent indexation is constrained. If weaker wage growth is expected, employee turnover may increase in administrations that compete with the private sector for skilled labour.

With no compensation, the effect on incentives is more immediate: net income decreases and the relative attractiveness of civil service weakens. This may achieve budgetary savings in the short term, but at the same time may increase recruitment and training costs and accelerate the loss of human capital. Therefore, a one-year static fiscal outcome is not a sufficient criterion for assessment.

Risks in Fiscal Interpretation. The most significant methodological risk is double-counting. Additional personal contributions to the SSI and the NHIF cannot be treated as an independent fiscal gain when they derive from a budget-funded increase in the gross remuneration. Inaccuracies also arise if the total budgetary expenditure on the Personnel Fund is applied mechanically as an insurable base, as well as if the maximum insurable income is disregarded, which overstates the effect for higher remunerations.

It is equally important not to conflate cash-based and economic effects. A contribution to the UPF represents a cash outflow from the public sector, but at the same time creates a financial asset for the household. Likewise, the legal allocation of the contribution should not be assumed to be identical to its economic incidence—an assumption that is not supported by public finance theory.

Political and Economy Assessment. With regard to horizontal equity, aligning the formal social insurance regime for civil servants with that applicable to other employees is a consistent step. Individuals with similar incomes and comparable social rights are subject to a more comparable structure of gross and net remuneration. This enhances the transparency of public compensation for labour.

As an instrument of fiscal consolidation, the measure is considerably weaker if net income is fully compensated. In that case, the main outcome is a reformatting of remuneration and a redistribution of financial flows. A lasting saving arises only if part of the burden remains with the employee or if the compensation is combined with a constraint on future growth in the Personnel Fund.

The reform has a stronger rationale in terms of equal treatment, transparency, and institutional symmetry than as a standalone instrument for achieving significant budgetary savings. If the primary objective is fiscal, more direct instruments remain policies concerning headcount, remunerations, and indexation.

Recommendations for Budgetary Policy and Follow-up Assessment

First, the technical compensation for employee social insurance contributions should be accounted for separately from actual increases in remuneration. This makes it possible to measure the wages gross-up effect and to prevent it from being presented as a real increase in remuneration.

Second, it must be clarified through both regulatory and budgetary means whether the compensatory component is included in the base for future indexations, bonuses, and benefits. If it is included without constraints, the long-term cost of the reform may significantly exceed the initial estimate.

For the follow-up assessment, it would be necessary for the Ministry of Finance and the NSSI to publish annual data at least on the number of affected persons, the insurable income, the compensation expenditure, the employer and employee contributions by fund, the additional income tax, the flows to the UPFs, and the net consolidated effect.

A separate assessment is required for the judiciary, where the remuneration structure and the share of income above the maximum insurable income may differ substantially from those in the general administration. In addition, the analysis should cover at least the 2026–2028 period, as the actual effect also depends on future indexations and headcount policy.

4. Conclusion

The change in the social insurance model for civil servants constitutes a significant institutional reform, but its economic effect is more complex than the simplistic assertion that employees merely begin to pay their own social insurance contributions. From 1 August 2026, and particularly from 1 January 2027, an employee social insurance burden is indeed introduced. When the state compensates net income, the short-term economic burden remains largely with the public employer.

Without compensation, there are real budgetary savings, but these are achieved through a lower disposable income for employees. Under full compensation, the effect is predominantly distributional: the structure of gross remuneration, the revenues of the SSI and the NHIF, the tax base, and the flows toward the UPF change. The net consolidated outcome remains dependent on the specific wage gross-up effect, the maximum insurable income, and the income distribution.

The option in which compensation is combined with a restriction on the future trajectory of the Personnel Fund has the greatest potential for a lasting fiscal effect. In this case, however, the source of the savings is the personnel policy rather than the formal 80:20 or 60:40 ratio. This distinction is necessary for a proper academic and public assessment of the measure.

According to Musgrave (1959), the reform is primarily distributional and institutional. According to Stiglitz and Rosengard (2015), the distinction between legal and economic incidence is key, while Barr's (2001) analysis shows that a portion of current flows represents a transfer of resources over time through pensions accumulation. The combined use of these approaches provides a more comprehensive economic assessment than a purely accounting-based tracking of the payroll.

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