



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 30.12.2003  
COM(2003) 842 final

**COMMUNICATION FROM THE COMMISSION TO THE COUNCIL, THE  
EUROPEAN PARLIAMENT, THE EUROPEAN ECONOMIC AND SOCIAL  
COMMITTEE AND THE COMMITTEE OF THE REGIONS**

**Modernising Social Protection for More and Better Jobs  
a comprehensive approach contributing to making work pay**

## TABLE OF CONTENTS

1.	Introduction .....	3
2.	Need to modernise social protection policies.....	6
3.	Better social protection policies and labour market transitions .....	7
3.1.	From benefits to jobs: helping men and women to earn their own living.....	7
3.1.1.	Obstacles to the labour market integration of people living on labour market benefits .....	8
3.1.2.	Policy reform trends and employment-friendly measures .....	10
3.2.	Reconciling work and family life and supporting working parents.....	11
3.2.1.	Obstacles to the labour market integration of working parents .....	11
3.2.2.	Policy reform trends and employment-friendly measures .....	13
3.3.	From job to job: facilitating occupational and geographic mobility.....	14
3.4.	From incapacity to work: offering a new start for people with health problems.....	15
3.4.1.	Obstacles to the labour market integration of people with health problems.....	15
3.4.2.	Policy reforms trends and employment-friendly measures.....	16
3.5.	Prolonging working lives .....	18
3.5.1.	Obstacles to longer working lives in current social protection systems .....	18
3.5.2.	Policy reforms trends and employment-friendly measures.....	19
4.	The situation in acceding countries.....	20
5.	Policy lessons to be drawn .....	21

## 1. INTRODUCTION

In March 2003, the European Council invited the Commission "*to report in time for the 2004 Spring European Council on the improvement in the overall framework for social protection policies through a greater emphasis on the effectiveness of incentives (e.g. benefit systems, reconciliation of family and work life, measures for older people) and the identification of best practice*".

The main purpose of this Communication is to address the key challenge of promoting more effective work incentives in social protection systems while allowing them to pursue their central goal of providing a high level of social protection for all and, at the same time, avoiding excessive budgetary costs. This is a matter that has raised considerable political interest in all Member States, as most are making efforts in order to increase the levels of participation in employment. This is crucial in order to lift the long term threat that demographic ageing is posing to the financial and social sustainability of social protection systems. Increasing participation in employment, particularly among most disadvantaged people, is also seen as the main safeguard against drifting into poverty and social exclusion.

At EU level, the efforts made by Member States to review social protection systems in order to make them more employment friendly are supported and driven through strengthened coordination of economic, employment and social policies. Ambitious targets have been set at EU level for 2010: to increase the overall employment rate to 70%, the employment rate of women to 60% and the employment rate for people in the age range 55-64 to 50%. These targets are supported by various guidelines and recommendations included in the Broad Economic Policy Guidelines and the Employment Guidelines, as well as in the common objectives of the Open Method of Coordination in the areas of pensions and social inclusion. As part of the policy agenda for the modernisation of European social model, social protection systems need to be adapted in the framework of an active welfare state to ensure that work pays while securing their social policy goals such as fighting poverty and social exclusion. However, these objectives are not in contradiction with each other: the best safeguard against social exclusion is a job as it was stated in the Lisbon conclusions. There is therefore a transversal concern cutting across several areas of policy coordination and a need to move towards a more integrated approach, combining a focus on the role and functions of social protection systems, with the need to maintain appropriate incentives for people to get and maintain jobs, and adding a concern for the impact of equally relevant policies in the areas of labour market, health care and family support.

The decision to accept a job is influenced by financial as well as a wide spectrum of non-financial aspects. "To make work pay" has been used as a label for policies that aim at reforming tax and benefit systems with a view to providing appropriate financial incentives to take up jobs, to remain in work, to increase work effort and to invest in education and training. Such strategies are covered by Employment Guideline 8 and the Broad Economic Policy Guideline 4<sup>1</sup>. Both the Joint Employment Report and the BEPGs' Implementation Report analyse in detail efforts made by Member States in addressing this issue.

The BEPGS and the EGs as well as their Implementation reports will continue to cover the objective of 'making work pay' from the perspective of economic and employment policies. In particular, the Communication on Streamlining open co-ordination in the field of social

---

<sup>1</sup> See COM (2003)176 final and COM(2003)170 final.

protection<sup>2</sup> states that “both the economic and employment policy co-ordination processes address appropriate incentives to take up work, remain in work, increase work effort and invest in education and training. This implies in particular that they deal with the incentive effects of the interaction of tax and benefit systems, as well as of labour market policies”.

While the financial incentives embedded in benefit and tax systems are the core of policies to make work pay, also the non-financial incentives such as care services for children, disabled people and the frail elderly, job search assistance, training, health care, etc. have an important role to play.. Therefore, there is a need for a comprehensive approach dealing with a wide range of incentives, both financial and non-financial, that can support workability and employability and ensure that work pays.

The present communication identifies the main challenges and policy responses that Member States have implemented with the aim of making social protection systems more employment friendly. It has benefited from the replies submitted by the delegations to the Social Protection Committee in September 2003 to a questionnaire addressed by DG EMPL. The questionnaire focus on income support measures – including their tax treatment – for people of working age – including incentives for retaining older workers longer in employment – and on measures targeted at facilitating the reconciliation of family and work life. The communication draws upon a recent report on social protection and employment prepared by DG EMPL for discussion at the Social Protection Committee<sup>3</sup>. It also took into account the report by a Group of Experts working under the auspices of the Employment Committee<sup>4</sup>, focusing on the interaction between tax and benefits, which is a major issue in the debate on make work pay.

#### **BOX- Report to the Employment Committee on “Making Work Pay”-Group of experts on Making Work Pay**

*The report identifies the main factors underlying the (lack of) financial incentives to seek, take up and remain in work. It states that financial incentives determine to a large extent whether transitions on the labour market take place or not and that they therefore constitute an important allocation mechanism. In addition, the non-financial factors and the design of social security systems are important to make work attractive.*

*The report also analyses possible instruments for enhancing financial benefits from accepting work. Examples from Member States are used to illustrate policy options. The report focuses the attention on the fundamental trade-offs between the ability of low income support programmes to be effective in relieving poverty and to have well-targeted benefits while maintaining desirable work incentives and avoiding unsustainable budgetary costs. It is stressed that in designing policies to increase incentives for MWP, three aspects should be taken into account*

*1. Increasing labour supply: Unemployment traps, inactivity traps and low-wage (poverty) traps have an adverse influence on total labour supply and should be diminished in order to increase labour participation and employment growth and reduce benefit dependency. ./..*

*2. Poverty alleviation: Social security systems and income dependent schemes play an*

---

<sup>2</sup> COM (2003) 261.

<sup>3</sup> A revised version of the Commission document "Key Issues on Social Protection and Employment" was discussed by the SPC on 13 June 2003.

<sup>4</sup> The report by the EMCO Group of experts on "Making Work Pay" was discussed by the EMCO on 9 October 2003.

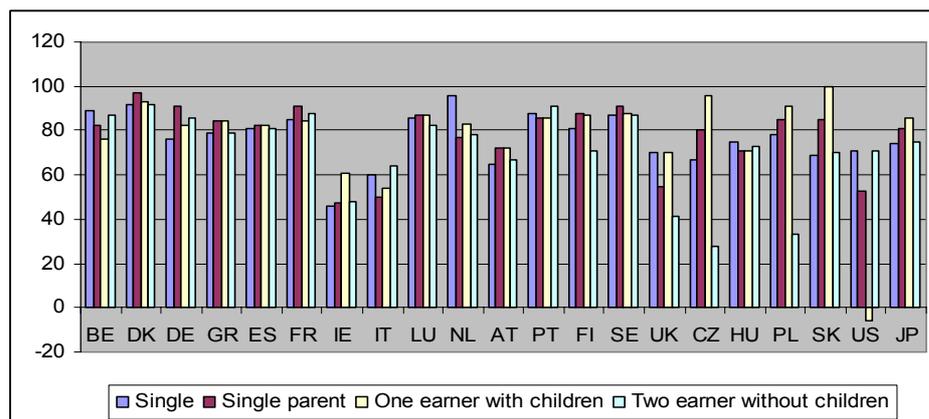
important role in the alleviation of poverty, by supporting low income families

3. *Budgetary cost: Measures to improve incentives for MWP should be cost effective and consistent with a broader budgetary framework.*

*These aspects form what is sometimes called a ‘challenging triangle’, because of the occurrence of trade-offs. Successful policies for Member States to make work pay have to find a proper balance within this challenging triangle.*

*The report analyses figures related to the three main indicators of low-wage (poverty) , unemployment and inactivity traps<sup>5</sup>.*

### **Unemployment trap indicator (on 67 per cent of the APW (2001))**



*The main results of the report were that when moving from an unemployment benefit situation to a job, around 80 per cent of the increase of gross income is not received by the employee in almost all Member States. There are some exceptions, where nevertheless still more than half of the gross gain is lost. Thus the unemployment trap is a serious problem in most Member States, as net income changes from leaving the benefit situation are low. With regard to the inactivity trap and the low-wage (poverty) trap the evidence is mixed. In some countries gross income gains do not result in net gains at all and thus are financially not attractive. In other countries more than half of a gross income increase is translated into a net increase. Overall, the report states that financial incentives are often lacking for people on unemployment benefit (unemployment trap), for people on social assistance (inactivity trap) and for those in low paid jobs to accept a better paid job (poverty/low-wage trap).*

*In the policy conclusion it is clearly argued that there is no single instrument to make work pay for everyone in every situation. Country specific circumstances largely determine the size and nature of the problem and the effectiveness of possible solutions. While the lack of financial incentives to make work pay generally derives from the interaction of schemes primarily designed for other purposes, mainly poverty alleviation, it is important that these policies with an impact on making work pay are mainstreamed and reformed, so as to reduce their adverse effect on labour supply. MWP-policies should be firmly embedded in labour market policies.*

<sup>5</sup> A detailed presentation of the methodology and the results of the joint project between the Commission services (ECFIN, EMPL, TAXUD, EUROSTAT) and the OECD for the calculation of low-wage, unemployment and inactivity trap is in the European Commission Economic paper n. 195, “Indicators of Unemployment and low-wage traps”.

## 2. NEED TO MODERNISE SOCIAL PROTECTION POLICIES

Social protection operates through a wide mutualisation of individual risks and achieves a more effective level of protection and better coverage than could be achieved through individual insurance. Social protection should provide a reasonable income replacement guaranteeing a decent living standard to people who cannot provide for themselves through employment. A variety of situations are covered which are characterised and checked through implementing provisions: sickness, disability, old age, unemployment, low income. The primary function of social protection institutions consists in providing security against risk and hazards of life. In fulfilling this function, tax and benefit programmes may have potentially distorting effects on the efficient functioning of the labour market.

Such distorting effects are usually described in the literature as inactivity, unemployment and poverty traps<sup>6</sup>. The *inactivity/unemployment trap* occurs when benefits are high compared with expected incomes from working and/or a substantial part of the earned income is taxed away when a person takes up work. The situation described as *poverty trap* usually arises when low-wage workers have little immediate financial incentive to increase hours worked or, in a household context, the spouse, normally the women, has little incentives to enter the labour market. Also, the incentive to work part-time or to invest in education and training to move up the wage ladder is blunted.

There is therefore a need for tax/benefit policies to be re-designed in such a way as to reduce the risk of inactivity, unemployment and poverty traps. In other words, a high level of social protection is desirable as long as incentives to work are maintained. There are no easy solutions to this problem, as reforming taxes and benefits to make work pay involves trading some policy goals against others. In such trade-off a relevant issue is the degree of choice afforded to individuals by the different types of institutions, and in particular the choice of individually based social security benefits vs. family – or household-based benefits –, an issue that is also important in relation to equality between men and women.

Modernising Member States' social protection systems by removing inherent disincentives to work and creating the right incentives and conditions for making work more attractive, is key to make them more employment friendly and hence to encourage higher levels of participation in employment. This will in turn contribute to make social protection systems more sustainable in the long run.

To achieve higher employment levels it is of paramount importance to support people in labour market transitions, i.e. when they are changing their labour market status, either because they are jobless and search for jobs, or envisage changing the type, the location or the nature of their job, or trying to move up the career ladder, or considering retirement. This Communication is structured in accordance with the different roles that social protection systems can play in promoting successful labour market transitions in five different labour market situations:

- From benefits to jobs,
- reconciling work with family life,
- from job to job,

---

<sup>6</sup> For measurement of these effects, see precise data in "Joint Commission-OECD project on calculating the effective tax rates on labour".

- from incapacity to work, and
- prolonging working life.

### **3. BETTER SOCIAL PROTECTION POLICIES AND LABOUR MARKET TRANSITIONS**

Following the approach described above, this chapter examines the interaction between social protection schemes and different labour market transitions. The aim is to identify strategies encouraging labour market participation through better activation of social protection. For each particular labour market transition, the obstacles to labour market integration faced by people receiving benefits are identified, including the role played by the eligibility criteria, its enforcement and, in general, the management of the benefit schemes. The analysis then moves to recent policy reforms adopted or envisaged with the aim of tackling such obstacles and making work pay. The analysis is supported by examples of good practice, making use of available information.

When discussing these different labour market transitions, the following types of benefit schemes are considered: (i) unemployment insurance and unemployment assistance; (ii) minimum income guarantee and other forms of social assistance (including housing benefits); (iii) employment-conditional benefits and other similar provisions; (iv) support for families and parents (family benefits, maternity, paternity and parental leave schemes, child-care benefits and provision, elderly care and care for disabled people); (v) early retirement; and (vi) support for sickness, invalidity and work-related injuries.

In approaching the range of policies that aim to make work more attractive, it is necessary to emphasise that financial reward is not the only and most important aspect determining job quality and work attractiveness. From the perspective of the worker a job that pays is one which provides the worker with both pecuniary (earnings, pension schemes) and non-pecuniary returns more or less subjectively defined as a result of a host of characteristics such as job status, employer behaviour, opportunities for education and on-the-job training, working hours, type of contractual arrangements, fringe benefits provided by the employer (pre-school childcare, training, health care, accommodation, etc.), distance travelled to work and commuting.

#### **3.1. From benefits to jobs: helping men and women to earn their own living**

Over the last decade there has been a re-examination across the Union of the role played by social benefits in encouraging jobless people to look actively for a job. While the attention has been focused on unemployment benefits and their impact upon those trying to re-enter the labour market after an unemployment spell, it has been extended to other welfare benefits particularly those subject to means testing. One has also re-examined the impact of benefits on those entering the labour market for the first time. Policy reforms have been prompted by the high rates of unemployment, and especially long-term unemployment, and a concern to ensure that social protection systems do not encourage people to delay re-entering employment or even to choose to live on benefits rather than to be employed. It has also been a response to rising labour taxes and social security contributions. However, in many instances, such reforms have raised public concern with their impact on the quality of work and the risk of poverty. As a result, they were implemented only after intense public debate and difficult negotiations with the social partners.

Several Member States have tightened up the qualifying conditions for eligibility, to increase the pressure on the unemployed to accept job offers, to develop effective means to counter

fraudulent claims and abuse of the systems and to shorten the period over which the benefits are payable. In some cases, such measures have resulted in a cutback of benefit levels. They have been applied not only to unemployment benefits but also to disability and early retirement schemes, which had come to be used as substitutes for unemployment compensation in a number of Member States, in the context of the industrial restructuring of the eighties, in recognition of the difficulty of many older unemployed people to get back to work.

Many Member States have increased investment in active measures to help those re-entering employment or acceding to it for the first time by improving their employability. This has involved typically supply-side measures such as training and individualised job search assistance, but in many cases these have been combined with measures, such as employment subsidies and reduced social security contributions aimed at creating a labour market demand for people carrying objective disadvantages (young people with poor education, disabled people, older unemployed, etc.). The latter aspect has been especially highlighted in the context of policy strategies aimed at developing more inclusive labour markets, where getting a job is seen as the safest way of ensuring the social inclusion of people at the risk of poverty and social exclusion.

The review of benefit systems has also been combined in an increasing number of countries with attempts to make work more rewarding financially by introducing measures that increase adequately the net income of those taking up a job, relatively to what they would receive in benefits, by allowing them to continue to receive some income support or by reducing the tax burden on low-paid workers. These measures have been directed in particular to encouraging people to take low-paid or part-time jobs, which they might otherwise be reluctant to do if the earnings they received were just marginally higher than the benefit amount.

### *3.1.1. Obstacles to the labour market integration of people living on labour market benefits*

Unemployment benefits perform an important role in protecting unemployed people against temporary loss of income during an unemployment spell. In addition, they contribute to a more efficient job matching by creating conditions for the unemployed people to select job offers criteriously and avoid rushed decisions. They also perform an important macroeconomic role by helping to maintain aggregate demand during a recession or economic slowdown. On the other hand, unemployment benefits may create disincentives to work, to the extent that they are paid over a long period and are not adequately monitored or controlled by means of clear requirements on active job seeking, work tests and participation in active labour market policy programs.

In most Member States, the underlying approach to address the risk of such disincentives has consisted in tightening up the conditionality of the benefit receipt upon job search and other relevant activities. One increasingly popular measure has been to get the personal involvement of the unemployed by conditioning the entitlement of the benefit to the signature of a contract in which the person involved is committed to undertake certain activities. These activities may vary from actively searching for work, training, achieving work experience with a voluntary organisation or on an environmental task force, or acceptance of a suitable job offer by the Public Employment Service. However, such an approach has to be carefully monitored in order to avoid that the reduction or suppression of benefits set off a pathway to poverty and social exclusion. Of particular concern is the fact that, despite the income

replacement mechanisms in place, 39% of the unemployed people in the EU lived at the risk of poverty<sup>7</sup> in 2000 (44% for men and 33% for women).

Social protection systems also influence the availability for work through a particular feature: Means testing has been growing in importance in a number of Member States, in an attempt to limit the growth of social protection expenditure, while at the same time concentrating resources on those most in need. (i.e. those households with income below a certain threshold). According to ESSPROS data, expenditure subject to means testing accounted for around 10% of total social protection spending in the EU in 1999, but in Ireland it amounted to almost 28% of the total and in the UK to 17%. The growth of means testing has affected a wide range of social protection schemes and in particular housing benefits, social assistance, unemployment benefits and disability benefits.

The problem with means testing is that it creates an artificial threshold that, once exceeded as a result, for instance of taking up a job, may induce a sharp cut in benefits which may leave the household in question with marginally higher or lower net income than before the transition from welfare to a job has taken place. A similar problem is created by the introduction of employment conditionality into certain welfare payments, for instance when the access to higher child allowances is conditional on one of the parents being unemployed. In recent years, some Member States have attempted to deal with the particular disincentives created by means testing and employment conditionality in the design of some welfare benefits. Ireland, for instance, has removed or reduced the financial disincentives to take up employment through *inter alia* freezing the absolute level of child dependant additions to the allowance and increasing the level of universal child benefit payment, and introduced transitional arrangements whereby benefits are paid on a sliding scale to further encourage people to take up employment. The housing benefits in France penalise the exit from the "Revenu Minimum d'Insertion" (RMI) as it involves a substantial decrease in income, particularly important for part-time jobs paid at the minimum wage level. As a result, the 1991 reform of the housing benefits aimed at suppressing this distortion which discouraged the transition from the RMI into work.

More generally, Member States have focussed their attempts to tackle disincentives created by social protection systems through the use of tax-credits, the possibility to combine benefits and work, and allowing a more favourable social security and tax treatment. While it is believed that these measures have had an impact in reducing the METRs (Marginal Effective Tax Rates), there is clearly a deficit in the evaluation of such policies, both in terms of their impact on employment and on short and medium term budgetary costs and returns. Few Member States provide the number of people who benefit from a specific scheme or the estimated reduction in marginal rates or the budgetary effort inherent in their support schemes aimed at making work more attractive<sup>8</sup>.

While not formally part of social protection systems, minimum wage policies are implemented by several Member States in order to face the problem of the working poor. If set sufficiently above the level of unemployment and other related benefits the minimum wage may increase the attractiveness of low-paid jobs and hence contribute to make work

---

<sup>7</sup> Risk of poverty is defined as living in a household with an equivalised income below 60% of the national median.

<sup>8</sup> This is the case for France, which to improve the financial incentives to work, reformed the housing tax in 2000, introduced a tax-credit (Prime Pour l'Emploi) in 2001, and allowed the combination of work with benefit receipts for a wide range of schemes. While the budgetary impact of these three measures was estimated at €4 billion, the disposable income of these households increased by around 3% allowing for a reduction of more than 4 pp in the highest marginal implicit tax rate.

pay. However, with a view to avoid affecting labour demand negatively and, thus, reducing job opportunities, additional measures have been undertaken in some Member States in order to compensate employers for hiring low-productivity workers at a cost above the hypothetical free market rate.

### *3.1.2. Policy reform trends and employment-friendly measures*

Guided by the activation principle embedded in the European employment strategy, Member States have introduced a wide range of measures aimed at avoiding that unemployment support schemes may create disincentives to work while, at the same time, encourage people in unemployment to take a job. Some of these measures work through the labour demand channel while others act directly on labour supply. The measures implemented could be grouped around three major categories: (i) employment incentives; (ii) combination of benefits and work; and (iii) more favourable social security and tax treatment.

- (1) Concerning employment incentives (labour supply channel), measures implemented by Member States have focussed on: (i) limiting the amount (Spain) or the length (Germany) of the unemployment benefit that can be perceived; (ii) unifying the unemployment insurance with the social assistance benefits; (iii) giving incentives for young people (Finland) or for new hires covering youths and adults over 25 who had not been employed on a permanent basis (Italy); (iv) making conditional activation complements (subsistence allowance) to job search and participation in active measures after a certain period of unemployment (Finland); and (v) using in-work benefits, i.e., employment conditional tax-credits and benefits and other provisions of similar purpose. On in-work benefits, several Member States used in the past, and have recently introduced, direct financial incentives to make work pay namely under the form of tax-credits. Looking at the number of people who came back to work after they benefited from these tax-credits, experiences in Member States look encouraging. However, an important disadvantage of these schemes lies on the fact that they could draw to the bottom the wages that employers are willing to pay. Another disadvantage is that in some cases (the Netherlands) the minimum benefit level is linked to the minimum wage, therefore, the financial incentive to accept a job paying the minimum wage tends to be low.
- (2) The second strand of policy followed by Member States refers to the possibility to combine the receipt of the benefit entitlement with earnings from work (labour supply channel) by allowing the following: (i) combination of part-time or full-time job with partial unemployment benefit or unemployment assistance (Spain, Ireland, Portugal) or with a wide range of other social benefit schemes such as normal and specific unemployment benefits, RMI, lone-parent allowance, ASS and disabled adult allowance (France); and (ii) incentives to start-up business or to encourage self-employment by allowing to receive the unemployment benefit in a lump sum payment (Spain).
- (3) The third strand of policy concerns the provision of a more favourable tax and social security treatment for both employees (labour supply channel) and employers (labour demand channel). As this Communication does not discuss policy measures affecting labour demand, the following measures only reflect those implemented by Member States aimed at influencing labour supply: (i) more favourable tax treatment for older workers deciding to prolong their working life (Spain); (ii) reform of the housing taxes not to penalise the entry in the labour market, namely of low income households, and total exemption for recipients of the RMI (France); and (iii) partial reduction or

exemption of social security contributions paid by targeted groups of employees such as those working in painful conditions, disabled, etc. (France, Portugal).

### **3.2. Reconciling work and family life and supporting working parents**

Public support for the reconciliation of work and family life has two aims. Firstly, family benefits aim to help families as they perform tasks which are fundamental to the very organisation and perpetuation of society. In particular, this involves supporting families as they give birth to, nurture and educate children and as they care for dependent family members, most notably sick, disabled or elderly dependants. In the context of demographic ageing, these policies are becoming more important as a means to reverse the declining fertility rates. Member states typically provide some of these supports in the form of universal benefits, e.g. child benefits, but with some supports made contingent on the family situation, e.g. lone parent payments, or paid in conjunction with other benefits, e.g. supplements for dependent children paid with unemployment benefits.

A second set of policies aim to make it easier for men and women to perform their family responsibilities while accepting a job or remaining active on the labour market. Thus subsidised or publicly provided childcare helps to keep people active in the labour market at times when family responsibilities could otherwise cause them to withdraw<sup>9</sup>. Maternity, paternity and parental leave allowances support temporary withdrawal from work. They are associated in a number of countries with provisions to ensure that attachment to the labour market is maintained. Other public supports aim to compensate people during those periods when they choose to leave the formal labour market to provide care within families. This compensation may take the form of cash benefits, e.g. carers' allowances, and/or credited contributions to pension rights which limits the disadvantage that the person concerned suffers in terms of pension entitlement. Some systems also offer specific activation supports to men and women returning to the labour market after a family-related absence to counter the effect that a break from employment may have on their employability.

The aim of this second group of provisions is to allow men and women to combine their family roles with labour market participation and to ease the transition between employment and full- or part-time in-family caring and vice versa. They also have a strong objective in terms of the promotion of equal opportunities between women and men in the labour market. They are both a reinforcement of, and a means to actively promote, high levels of employment participation. Typically they are most developed in those countries where there are high levels of female (and overall) participation in work.

#### *3.2.1. Obstacles to the labour market integration of working parents*

It is important that the mechanisms used to pay family benefits should not adversely affect work incentives. Insofar as child benefits are paid universally, this will not be a problem. However, the payment of family supplements in respect of children or dependent spouses as part of unemployment benefits, as is the practice in most Member States, may weaken further the financial incentive to take up work as discussed in Section 3.1.1 (note the discussion there regarding how Ireland has recognised and sought to address this issue).

---

<sup>9</sup> The primary importance of childcare as a support to the work participation of parents is borne out by Council Recommendation 92/241/EEC of 31 March 1992 which urged Member States to "take and/or encourage initiatives to provide childcare while parents are working, are following a course of education or training in order to obtain employment or are seeking a job or a course of education or training in order to obtain employment."

Furthermore, mechanisms for unemployment compensation should take account of the impact on the incentives for all members of a family. Where benefits are means-tested and the family's rather than the individual's income is used as the basis of assessment to entitlement, there may be a negative impact on the financial incentive both for the claimant and the claimant's spouse to take-up a job.

The non-availability of affordable child-care is seen as a key barrier to the participation of parents, in particular women. The costs of child-care services, the availability of the different types of child-care, the compatibility between hours of availability and working hours, the quality and the number of places are cited as important issues. This is particularly so at the lower end of the wage scale, among women and men with the lowest education and skill levels. There is evidence that the supply of such labour is sensitive to childcare costs. Accordingly, subsidies to reduce the costs of childcare services can help persons to return to work, including to part-time work. Although the direction of causality is unclear, several studies show that an extension of child-care support can increase in particular women's labour force participation.

The key role of the provision of child care in promoting participation in employment particularly of women, was recognised by the European Council of Barcelona, by inviting all Member States to provide child care by 2010 to at least 90% of children between three years old and the mandatory school age and at least 33% of children under three years of age.

Lone parents – whose numbers are increasingly significant in most Member States – are widely seen as being particularly vulnerable to barriers to their employment participation and, may accordingly face high levels of unemployment, dependency on income support and/or risk of poverty. The importance of the issue is also underscored by survey evidence that risk of poverty is highest among single parent households (35% for the EU average according to the most recent data from the European Community Household Panel survey), most of which are headed by women. In the United Kingdom, the exposure to the poverty risk for single parent households, which represent a relatively high proportion of all households, is particularly high at 50%. The UK has also set out its concern with the long duration of benefit dependency among lone parents.

The lack of access to affordable and suitable child care is likely to pose particular problems for this group. There is also considerable policy debate about how to balance the provision of adequate income support to lone parents, while preserving the incentive for a return to the labour market.

Maintaining work participation in the face of the possible disruptions related to family life is also seen as an issue of concern. This explains why various short leave schemes have been developed as a complement to the more long-term and developed forms of parental or care related leave. Examples include: in the UK, working parents are entitled to take time off work to deal with emergency involving a dependant ("Time off for dependants" scheme). In Portugal, pensions accruals are maintained for a person that decides to take part-time job to assist the child or adopted child and a short leave (15 days) to support a frail member of the family. In Sweden, temporary parental benefit is payable to parents caring for a sick child.

While the opportunity to take paid maternity leave may increase women's attachment to the labour market, a lengthy long-term leave is likely to increase the difficulties and uncertainties for women to return to employment, namely for those with insecure employment status or

with low skills and low pay<sup>10</sup>. The same comments apply for other forms of leaves such as parental leave. A comprehensive family-friendly policy helping parents to efficiently combine family and work would help alleviate the negative effects of a single leave provision isolated from the employment context.

### 3.2.2. *Policy reform trends and employment-friendly measures*

There is evidence of a continued high rate of investment in childcare in Nordic countries. In Finland, every child under school age has the right to municipal day-care once the parental allowance period ends, regardless of income level of the parents or of whether the parents work. In January 2002, Sweden introduced a ceiling on childcare fees as well as a maximum fee for child day care services. This fee cap will prevent increased childcare costs when parents increase the number of hours worked, namely for those going from unemployment to employment. From 2002, there is a guarantee for 3 hours/day child care for children of unemployed parents and of mothers having a second/further baby, in order to give parents of small children better opportunities to seek and take up work.

As from 2004, France will launch a number of measures to improve and simplify the system of family allowances. A new allowance called *Prestation d'Accueil du Jeune Enfant (PAJE)* will focus on low income families and will raise the benefit amounts. It will also allow a higher compensation if the beneficiary takes a part-time job. These benefit improvements will be matched with measures to increase the supply of childcare places. 20 000 new childcare places are planned by the year 2007. A tax credit will be created for those companies spending in favour of the child care needs of their employees.

In April 2003, the UK introduced two means tested schemes, the "Child Tax Credit" and the "Working Tax Credit" (WTC) to replace previous tax credits. They have the twin stated aims of helping to eliminate child poverty and to make work pay. The "Child Tax Credit" is the main way that families get money for their children and for 16-18 year olds in education. It replaces the old tax credits and benefits with a single system and is paid directly to the main carer. The WTC supports working people, including the self-employed, helping to top up earnings. It includes a child care element, which helps with the cost of registered or approved child care, which is paid directly to the main carer. However, for couple households there is still a claw back rate of 50 to 60% on additional earnings over and above childcare costs. The UK's in-work benefit scheme – which has been extended now to couple households without children – is in fact primarily focused on reducing the number of households that are dependent upon benefits. The result is that although this scheme provides incentives for the main breadwinner in couple and in lone parent households to enter employment, it has a negative incentive effect on the employment second earner in couple households, and has been identified by the OECD<sup>11</sup> as having lowered the employment rate of married women with working spouses.

Member States have devoted much attention to the balance to be struck when determining the conditions under which lone parent benefits are granted. These payments have often been paid without a requirement that beneficiaries are available for work. Nevertheless, Member States are seeking to strengthen the incentives and supports for participation in work. For example, in France, lone-parents are granted the *Allocation de Parent Isolé (API)* which provides a minimum familial income to those lone-parents having or expecting to have children. The API allowance is not conditional on participation in the labour market or on integration

---

<sup>10</sup> "OECD Employment Outlook. Towards more and better jobs". OECD, Paris, 2003.

<sup>11</sup> "OECD Employment Outlook. Towards more and better jobs". Op. cit.

measures, but does allow for the temporary combination of earned income from work, as an incentive to enter the labour market. In the UK, policies towards recipients of lone parent payments are stated to be based on persuasion towards participation in work and on granting of incentives, rather than on the strengthening of the formal obligation to seek work which has been general throughout their New Deal reforms of recent years. The stated objective in relation to lone parent is to help stop them from being economically inactive and to start looking for work. Interviews, aimed at rekindling an interest in the world of work, are mandatory.

### **3.3. From job to job: facilitating occupational and geographic mobility**

Occupational and geographic mobility is crucial for a high level of economic efficiency. Mobility helps companies to adapt to rapidly changing market environments and it allows workers to move to those activities where they can be more productive and achieve higher earnings.

Occupational mobility can take many different forms, ranging from the move between two jobs within the same organisation to setting up a business after having worked as an employee. Social protection systems can create obstacles to mobility, notably in those cases where mobility results in the reduction or loss of certain entitlements. However, social protection systems can also support mobility in many ways, for instance by assisting individuals in their professional shift (including through sabbaticals), contributing to the temporary cost of re-location or cushioning to some extent the risks involved in a new professional venture.

Historically, social protection systems were developed nationally by branches, groups of companies or types of employment. As a result, and while most important social protection schemes in the Member States presently tend to cover the entire country, there are many special schemes notably for civil servants, the self-employed and farmers which may make it difficult to move between these sectors. In particular, a move into self-employment in some Member States goes hand in hand with less comprehensive social protection against income loss and/or illness. Mobility requires bridges between these schemes so as to ensure that acquired rights to a pension or to a health or invalidity insurance are not lost and have to be built up from scratch.

Private and supplementary social protection arrangements are still often uncoordinated, meaning that it is difficult or even impossible to transfer one's rights from one scheme to another. This is particularly the case for company pension schemes where a change from one employer to another can result in a significant reduction in prospective pension entitlements.<sup>12</sup> It is therefore important to ensure that those who change jobs or interrupt their careers face better conditions for the acquisition, preservation and transfer of occupational pension rights.

At the EU level, the co-ordination of statutory social security schemes through Regulation 1408/71, notwithstanding its complexity, has been important in ensuring that workers are able to exercise their right to move freely in an EU-level labour market, although only a small proportion of Europe's total labour force make use of this right. No equivalent EU instrument exists as yet for private supplementary pension or health insurance.

---

<sup>12</sup> See the consultation document adopted by the Commission on 12/9/2003 "Improving the portability of supplementary pension rights second stage consultation of the European social partners" (SEC/2003/916) for further details on obstacles to mobility arising from occupational pension schemes.

Mobility often involves shifting from part-time to full-time work or vice-versa. The share of part-time work is still increasing in the EU and about one third of all new jobs created are part-time jobs. They can be particularly important as a pathway to full-time employment after a spell of unemployment or after a career break for family reasons or as a pathway to retirement. Social protection arrangements sometimes hinder such transitions, for instance where pension schemes base benefit entitlements on final earnings or social security coverage is limited by a threshold in terms of the number of hours worked.

Education and training in a lifelong learning perspective have an essential role to play in promoting occupational as well as geographic mobility. Specific measures for action at both national and European levels were proposed in the Commission's action plan on skills and mobility (February 2002)<sup>13</sup>, complementing the European Employment Strategy, the "Education and Training 2010" process, and the Copenhagen process on enhanced cooperation in vocational education and training<sup>14</sup>. The forthcoming Communication from the Commission on European Employment Mobility reports on progress made and makes recommendations for future action.

Finally, transforming undeclared work into regular work is also an important pathway with implications for raising competitiveness, improving the sustainability of the social protection system and promoting social cohesion.

### **3.4. From incapacity to work: offering a new start for people with health problems**

Incapacity reduces labour supply significantly, particularly among workers in their 50s and 60s. In some Member States up to one fifth or even one quarter of people in the age groups 55-59 and 60-64 are on invalidity benefits and outside the labour market. Many people who claim incapacity benefits would clearly be able to pursue some gainful activity. In the UK, it has been observed that 90% of all new claimants of incapacity benefits want and expect to go back to work in due course.<sup>15</sup>

There are many ways in which health problems can make it difficult or even impossible to continue exercising one's current occupation, either temporarily or permanently. If the incapacity is temporary, social protection systems should support a rapid return to the previous occupation by offering high-quality medical rehabilitation services. Permanent incapacity to work in one's previous occupation does not imply an incapacity to do any work at all. Modern labour markets offer a wide range of jobs with very different demands on the physical and mental abilities of the job holder. Thus, if a worker has to give up his previous job for health reasons, vocational rehabilitation measures should be considered in addition to medical measures so as to facilitate a speedy reintegration into the labour market. Social protection systems are a major determinant of whether people with health problems find their way back into the labour market.

#### *3.4.1. Obstacles to the labour market integration of people with health problems*

Invalidity benefit schemes are often based on a clear-cut categorisation of people into two groups: the able-bodied and the incapacitated or disabled. In a number of schemes, a benefit entitlement arises when the worker's earnings capacity is reduced, due to health problems, to

---

<sup>13</sup> COM (2002) 72

<sup>14</sup> See also the Communication from the Commission on the draft interim report "Education and Training 2010: the success of the Lisbon Strategy hinges on urgent reforms" COM (2003) 685 final.

<sup>15</sup> It should be noted, however, that this also reflects the particular nature of the benefit which is not just targeted at people assumed to be permanently incapacitated, as is the case in several Member States.

one third or less of that of an able-bodied worker. In some cases, this earnings capacity is assessed on the basis of earnings in one's previous occupation for a person with a similar qualification; in others it is simply the capacity to earn a decent living that determines eligibility for invalidity benefits.

The tendency in many invalidity benefit schemes is clearly to focus on incapacity rather than the remaining capacity to work. Invalidity benefits are typically passive benefits for those regarded as unsuitable for employment. Beneficiaries may be discouraged in various ways from offering their remaining work capacity on the labour market. Certain activities may be subject to prior approval by the benefit institution. If they are approved, benefits may be suspended or reduced, depending on the level of earned income. Thus the financial incentives to pursue a gainful activity tend to be weak. Moreover, beneficiaries may be reluctant to show their willingness and ability to work if it is too difficult to return to benefits should the labour market participation turn out to be unsustainable in the long run.

From the employer's point of view, hiring a disabled person can have several actual or perceived drawbacks. The workplace may need to be adapted, the disabled worker's productivity and flexibility might be lower (or perceived to be lower) and there may be fears that a disabled worker may be more often absent for health reasons. The shift of the cost burden of illness from social insurance (sickness cash benefits) to employers that has taken place in some countries (e.g. Netherlands) may increase the reluctance of employers to recruit disabled workers.

The importance of invalidity benefit schemes as a factor that objectively reduces participation in employment is compounded by the use of eligibility criteria other than objective medical criteria. In many cases, the definition of invalidity may be relative to one's prior earnings capacity which depends on one's occupation and qualifications and even on the region of employment. The labour market situation and hence the chances of finding a suitable job may also be considered in awarding invalidity benefits.

### *3.4.2. Policy reforms trends and employment-friendly measures*

Early intervention is often the best way of preventing long-term benefit dependency. This implies speedy access to medical care that can prevent incapacitating health problems or that rehabilitates those who are already experiencing serious problems. If the deterioration of the health status cannot be prevented or reversed, thus making a change in occupation necessary, vocational conversion must be envisaged. Such measures are foreseen in most social protection systems, often in various branches (pension insurance, unemployment insurance, health care, accident insurance).

In Finland, a right to early vocational rehabilitation measures for people at risk of becoming disabled is being introduced. The scope of vocational rehabilitation paid for by the pension system has expanded continuously. Results of this policy in Finland are encouraging. It has been shown that rehabilitation measures are self-financing because they tend to prolong working lives by more than two years on average. The best rehabilitation results are achieved when rehabilitation is launched at a sufficiently early stage and well targeted. This requires of course a good cooperation between all the different actors involved.

In the Netherlands and Luxembourg, there is an obligation on employers to find a more suitable job for a disabled person within the company (if it has more than 25 employees, in the case of Luxembourg) or, in the case of the Netherlands, also in another company. France seeks to promote the employment of disabled workers through a quota system which obliges companies with more than 20 employees to employ at least 6% of disabled workers or pay a

contribution. In Luxembourg, re-deployed disabled workers enjoy special protection against dismissals during one year. Such employment and redeployment obligations tend to be matched by support measures for the employer who may receive subsidies for adapting the workplace or for providing training.

Some Member States recognise partial invalidity, thus accommodating, to some extent, the diversity of incapacity conditions. Sweden distinguishes four levels of reduced work capacity: 25%, 50%, 75% and 100%. Beneficiaries of partial invalidity benefits are encouraged to use their remaining work capacity. A distinction between full and partial invalidity benefits also exists in Germany and is being considered in Austria.

Even in the absence of partial invalidity benefits it may be possible to receive earned income alongside an invalidity benefit. Such earnings are usually subject to an earnings ceiling which may depend on earnings before the onset of invalidity; thus, in France the ceiling for the combined income is the level of earnings before invalidity. An exception with regard to ceilings is the German accident insurance scheme which pays pensions as a compensation for a permanent medical impairment suffered as a result of a work-related accident; such pensions are paid regardless of any other income.

In order to overcome the reluctance of invalidity benefit recipients to take up work, Sweden and Finland allow beneficiaries to suspend their entitlement temporarily to test their ability to work. This period can be between six months and five years in Finland; during the first two years of employment a supplement is paid. Sweden allows a trial period of two years without losing the benefit entitlement and continues to pay benefits during the first three months of employment. Ireland offers a 'back-to-work' allowance which allows beneficiaries to retain their benefit entitlement for three years (four in the case of self-employed) while taking up full-time employment.

Many countries are reviewing the conditions of eligibility to invalidity benefits by focusing less on labour market considerations and applying stricter medical criteria. As a result, Luxembourg managed to reduce the number of new disability pensions by half between 1996 and 2000. Poland introduced in 1997 stricter rules for medical invalidity assessment by shifting these tasks from doctors' committees to the social security (ZUS) doctors and France has announced that it will reinforce the effectiveness of medical controls. However, in the absence of effective labour market integration measures targeted at people with disabilities, the tightening of the eligibility criteria, be they medical or economic and social, could result in shifting the burden from invalidity schemes to other branches of social protection, namely unemployment, sickness, early retirement and social assistance.

Finally, it is still widespread to grant subsidies to employers, often in the form of reduced social insurance contributions, in order to support hiring or maintenance at work of disabled people. Denmark, for instance, developed the concept of 'flexi jobs' for people with permanently reduced work capacity; wage subsidies to the employer amount to between  $\frac{1}{2}$  and  $\frac{2}{3}$  of the salary. Financial incentives may be backed up by extensive on-the-job support through individual job coaches who can be employed by either the employer or the community (Austria, Denmark, Germany, and UK). An option for providing employment opportunities for the most severely disabled consists in offering special employment in a sheltered environment, be it in special workshops or businesses or in protected segments in ordinary companies. The Netherlands and Poland have put particular emphasis on this approach.

### **3.5. Prolonging working lives**

The Stockholm European Council set the ambitious goal of raising the employment rate of people aged 55-64 years to 50% (standing at 40.1% in 2002 and as low as one quarter for people aged 60-64). The Barcelona European Council introduced a complementary ambitious target of increasing by five years the average age of exit from the labour market by 2010 (currently at 61 years, according to the estimations of Eurostat). Achieving these goals will be crucial for ensuring the future financial sustainability of social protection and notably for guaranteeing adequate level incomes for future pensioners.

Increased participation of all ages in the workforce requires promoting active ageing through the positive interaction of economic, social and employment policies, and a strong involvement from the social partners. Furthermore, it requires stronger investment in the quality of work by promoting measures to provide an attractive and adaptable work environment, improving access to training, and enhancement of work incentives for taking up or staying longer in employment. In this context, existing models of retirement and recruitment will have to change and the culture of early retirement should not be accepted as the preferred solution to downsizing and corporate restructuring.

#### *3.5.1. Obstacles to longer working lives in current social protection systems*

Social protection schemes certainly contribute to the current low employment rates of older workers as they offer various options for an early withdrawal from the labour market. Since the rise in unemployment in the mid-1970s, early retirement became a major tool for adjusting the labour force in companies. Social protection schemes made it easier, and socially more acceptable, to shed older workers rather than younger workers. In view of demographic ageing such a policy, that reduces the labour supply of people in the 50s and early 60s, is no longer sustainable. The Ageing Working Group of the Economic Policy Committee estimated that an increase in the effective retirement age of one year would reduce the expected increase in public pensions expenditure by 0.6 to 1 percentage points of GDP (assuming that the reduced incidence in early retirement does not give rise to additional pension entitlements). From the point of view of adequacy, too, it will be important to make pension systems more employment friendly: if individuals can increase their pension entitlement by working beyond the standard retirement age (either by combining earned income with a pension or by deferring the receipt of their pension) or opting for gradual retirement then this can make a major contribution to the future adequacy of pensions.

There are numerous ways in which social protection systems support the early exit of older workers from the labour market. Certain professions benefit from a lower retirement age justified by the fact that work in these professions is physically demanding. An alternative to early retirement for such groups would be to improve working conditions and to allow older workers in such professions to move on to different activities. People with long contribution careers may be eligible for a pension well before reaching the standard retirement age. This can be justified on grounds of fairness towards people who had to start working early in life – typically on low earnings –, but this should not prevent them from remaining longer on the labour market to achieve a higher retirement income.

Pension schemes often also penalise, in financial terms, those who want to work longer: by reducing pensions if the beneficiary has an income from employment or by denying an actuarial increment for those who claim their pensions later (and hence for a shorter remaining period of their lives). A retirement condition for the receipt of a pension and various means tests in pension schemes tend to discourage older people to remain on the labour market. There are many restrictions on the amount of income that can be earned in

addition to a pension. While the payment of the pension is sometimes suspended, in other cases there are deductions from the pension. Moreover, in the case of deferred retirement, the contributions paid by the worker and the shorter remaining life expectancy at the time of retirement is often not or only partially reflected in the pension level<sup>16</sup>.

Unemployment benefit schemes provide, in many Member States, another exit door from the labour market. Older unemployed sometimes get more generous benefits and they are often not required to be available and looking for work. In some Member States, invalidity benefits allow a significant proportion to retire early, depending on how easily such benefits are granted, on whether support is given to find a more suitable job and on whether the evolution of the health situation is regularly monitored.

### 3.5.2. *Policy reforms trends and employment-friendly measures*

Member States recognise that the EU target of raising the employment rate of people aged 55 to 64 and of increasing the effective average exit age must be supported by profound adaptations of their social protection systems. These reforms are now underway and they have the potential of increasing significantly the activity rates<sup>17</sup> of people in the 50s and 60s. While most Member States tend to concentrate on benefit reforms and are far from developing comprehensive active ageing strategies an increasing number stress the need to maintain the employability of older workers through lifelong learning, to provide better job search support, to adapt working conditions, to change attitudes and combat age discrimination and, in some cases, to lower the costs of employing older workers, notably by reducing social security contributions.

Several Member States are tightening the eligibility criteria for unemployment benefits while offering more support to older workers for finding employment. In Belgium, the older unemployed will be required to register as job seekers and obliged to accept work up to the age of 58 (instead of 57 previously). The Netherlands, are abolishing altogether the age limit above which job search is no longer required (currently 57½ years). Finland and Austria are closing their early retirement schemes for the unemployed, and Germany reduces the period of unemployment benefit receipt for older unemployed people. The implication of such measures is that older unemployed will no longer be regarded as definitively excluded from the labour market.

Early retirement is becoming more difficult even for people with long careers. In Spain, such an option mainly exists for people who had entered the labour market before 1967. Italy is gradually increasing the number of contribution years required for a 'seniority pension'. Retirement before the standard retirement age remains possible in many Member States, but only at the price of an actuarial reduction in pension benefits.

Gradual retirement, i.e. the combination of a partial pension with part-time working may be an alternative to an early complete exit from the labour market. Such option already exists or is being introduced in several Member States. Its effect is, however, ambiguous: it may lead to an increase in employment participation if the alternative is a complete cessation of activity; or it can reduce labour supply if, in the absence of the partial pension option, workers would have continued to work full-time. Moreover, the conditions attached to the option of combining partial pension with part-time work will have to be made more attractive if it is to

---

<sup>16</sup> This implies that the 'net pension wealth' of an individual is reduced by deferring retirement.

<sup>17</sup> The activity rate is the proportion of people in the age group who are available and actively looking for work.

be adopted by a significant number of workers in the countries where this possibility exists (Germany, Belgium, among others).

A rise in the 'normal' retirement age starts to be envisaged in some Member States, often in the context of flexible retirement schemes. In Sweden this is a reality since the 1999 reform and the issue is openly discussed in Germany as a policy alternative. Austria and France are raising the number of contribution years required for a full pension. In France, this implies that an increasing number of people will have to continue working beyond the standard retirement age of 60 if they want to earn a full pension entitlement. The equalisation of retirement ages for men and women (e.g. Belgium, Italy, Portugal, UK) or between the private and the public sector (Austria, UK) will also contribute to a higher effective retirement age.

There is a clear trend towards allowing older workers to stay longer on the labour market and to combine earnings with their pension or, if they defer the receipt of their pension, to acquire higher pension entitlements. The possibility of deferring once pension is even considered in countries with flat rate basic pensions (Denmark, Ireland, and UK). Other Member States are introducing or improving the pension increments for people who remain longer on the labour market. However, a number of limitations on earnings for pensioners remain in place and constitute serious obstacles to continued labour force participation; they also deny older workers important opportunities for securing an adequate income in old age.

Closer links between life-time earnings (or contribution payments) and pension benefits have been or are being introduced in a number of Member States. This takes notably the form of considering not only the final years of a career in the pensions formula, with the result that workers who have lower earnings during the final years of their career (as a result of part-time working or a 'second career') will not suffer undue reductions in their pension rights.

Finally, Member States with significant occupational pension schemes will also have to monitor the impact of such often tax-privileged schemes on early retirement. Both the Netherlands and the UK are tightening the eligibility conditions for tax advantages for private occupational pension schemes offering early retirement pensions. In the UK, the accepted minimum age is to be raised from 50 to 55 years.

#### 4. THE SITUATION IN ACCEDING COUNTRIES

While the current problems facing social protection systems in Acceding countries greatly differ among them, the following features seem to be more widely present<sup>18</sup>: (i) *low participation rates*: with some exceptions, Acceding countries show low participation rates partly reflecting high unemployment and high dependency ratios, which result from the extensive use of early retirement and invalidity pensions used during the economic restructuring processes underwent in the 1970-80's. Further, some Acceding countries have more traditional social structures making the access of women to employment more restrictive and reconciliation of work and family life more difficult; (ii) *weak social protection and non-employment friendly tax systems*: despite current reforms, existing welfare systems are not very generous in financial terms, have loose eligibility conditions and provide weak access to social protection; this help develop a culture of making the necessary to live on benefits instead of directing efforts to search for a job. Finally, tax systems are sometimes ill prepared to develop an efficient tax collection, while taxation on labour is relatively high; and (iii)

---

<sup>18</sup> There are still too few analytical elements allowing an overview of the main obstacles to labour market participation related to the structure and functioning of social protection systems in Acceding countries.

*informal economy and migration*: while immigrants, either legal or illegal, increase the capital stock and, thus, the growth potential of these economies, they raise the problem of making work attractive for low-paid workers (legal immigration) and of transforming undeclared work into regular employment (illegal immigration). Legal immigration poses serious problems both in terms of coverage of these workers and for the long-term financial sustainability of the social protection systems in host countries.

Acceding countries should reinforce their social protection systems and active labour market policies, with the aim of reducing the dependency ratio of people living on long-term benefits, improving the employability of job seekers and increasing the participation rates, particularly of women and older people. However, in considering policies that prolong the working lives, account should be taken of the concrete circumstances prevailing in those societies, particularly with respect to the lower life expectancy, namely for men. Finally, on undeclared work which sometimes is related to the illegal economy, legal sanctions should be re-enforced and individually-tailored programs should be developed to make legal work pay for them.

## **5. POLICY LESSONS TO BE DRAWN**

Without prejudice of the policy recommendations to be given in the BEPGs and the EGs, the following conclusions can be drawn from this report as regards the contribution that social protection policies can provide to workability and employability:

- (1) Member States should review and modernise their social protection systems to make them more employment friendly by removing barriers and disincentives to work and create the right conditions to make work more attractive. While this may require the introduction of new instruments, significant improvement can occur just by reviewing existing policies with the aim of eliminating provisions in present benefits and tax schemes that have a negative impact on people's willingness or availability to take up a job or remain in work and reduce the tax burden on low-paid workers.
- (2) No single instrument or benefit scheme will suffice to make work attractive. Therefore, Member States should examine the interrelationship of objectives in policy areas such as taxation, social security systems and income dependent benefit schemes when implementing policies to make work more attractive. While there is a tendency to implement making work pay policies by applying a piecemeal approach, Member States should develop a comprehensive strategy combining social objectives with the economic, employment and budgetary objectives, as underlined in the Employment Guideline 8 and the Broad Economic Policy Guideline 4. Moreover, there is need for closer co-ordination between the different agencies and bodies responsible for implementing interrelated reforms.
- (3) Member States should consider non-financial incentives in conjunction with financial incentives. When designing social protection reforms, Member States should also place particular attention on aspects that have proved to be effective incentives to work – in addition to financial incentives – such as the following:

- (a) the provision of adequate (affordable and high quality) facilities for the care of children and other dependent people, like older and disabled relatives;
  - (b) the quality of work, as determined by such factors as flexible working hours, training opportunities, job security, adequate social protection coverage.
- (4) In reviewing social protection policies with the aim of making work pay, particular attention should be placed on the interaction between passive benefit schemes and active measures, notably in relation to job search and training. Stricter conditionality can help addressing the financial disincentive to work inherent in the tax-benefit systems without necessarily reducing its generosity (i.e., the duration and level of replacement income). As part of the efforts to improve incentives to work, it is important to avoid that stricter conditionality, particularly when imposed on social assistance benefits, may put particularly disadvantaged people at a serious risk of poverty and social exclusion.
- (5) When evaluating the cost-effectiveness of benefit schemes, Member States should carry out a more thorough and systematic analysis of the implications, and consider also the medium-term impacts. In particular, well designed measures aimed at bringing people back into the labour market or prolonging their working lives can be beneficial for both the individual and the society as a whole.
- (6) Removing barriers to geographical and occupational mobility is an important objective but progress has been slow. Hence, policies to overcome such barriers need to be boosted. Member States need therefore to focus more attention on promoting mobility in the labour market, for instance, moving from part-time to full-time work, moving to self-employment or moving to gradual retirement and from undeclared work into regular employment. Specific actions may include financial incentives support schemes such as mobility grants and training and legislative measures. The role of education and training in a lifelong learning perspective is also crucial in this respect.
- (7) Finally, Member States should ensure that supplementary social protection schemes, as they become an important element of social protection, are designed in such a way that they do not hinder workers in their mobility and advancement of their careers.