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### In-work benefits and their role in supporting employment

#### Introduction

Work is the best way to ensure self-sufficiency, professional development and access to work-related social-protection provisions. Current shortages of labour and skills across the EU Member States are acting as a bottleneck for economic growth. They are a serious challenge hindering business development by putting additional pressure on labour markets.

Labour shortages are structural in nature and aggravated in the short-term by consecutive waves of the Covid lockdowns. As a result, a growing number of companies do not find people for jobs they create as they depend on a shrinking number of working age workers and the available workforce does not possess the skills required by these jobs.

At the same time a significant number of working age people remains inactive: one in four working age people in the EU is inactive, while the inactivity rate exceeds 30% in four EU Member States<sup>1</sup>. There is an urgent need to bring people (back) to the labour market and well designed in-work benefits are an important tool towards this objective.

#### In-work benefits: definition and role

In-work benefits (IWB) are at **the core of making-work-pay policies** and improve work incentives. IWB are supportive for job creation as they increase disposable income, while not raising the cost of work for employers. IWB also support employment by contributing to job retention and making low-paid jobs more attractive. Additionally, they top up incomes of the most vulnerable groups of workers and contribute to better economic situation of their households.

OECD defines IWB as “permanent work-contingent tax credits, tax allowances or equivalent work-contingent benefit schemes, designed with the dual purpose of alleviating in-work poverty and increasing work incentives for low-income workers”.

The impact of IWB is different across various salary groups. **Low-income workers are more responsive to financial incentives** than the middle or high-income earners. As a result, IWB targeted at low-income workers tend to result in important positive employment effects. Moreover, IWB are an interesting policy option due to their relative cost-effectiveness.

#### At a glance: IWB across the EU<sup>2</sup>

All EU Member States provide IWB schemes. However, the dispersion of IWB in-work across EU Member States is not even and regional variations are observed.

The initial mapping of IWB for 2016 proves that most of the EU Member States had in place at least one of the following IWB sub-types: in-work cash transfers, adjusted unemployment benefits and earned income tax credit (including both refundable and non-refundable earned tax credits). The table below presents the overview of IWB by these three sub-types and how it evolved between 2008 and 2016.

<sup>1</sup> These are Croatia, Romania, Greece and Bulgaria.

<sup>2</sup> Based on Abbas, J. (2020), [What role for “in-work benefits”? A comparison of policies in EU Member States, 2006-2017](#), Ph.D. thesis, University of Bath, pp. 120-126.

Table 1. IWB across the EU: by sub-type (2008 and 2016)

|                                 | Number of EU MS | Proportion of EU MS | Proportion of EU MS with IWB |
|---------------------------------|-----------------|---------------------|------------------------------|
| <b>2008</b>                     |                 |                     |                              |
| MS with IWB                     | 17              | 63%                 | 100%                         |
| • In-work cash transfers        | 3               | 11%                 | 18%                          |
| • Earned income tax credits     | 12              | 44%                 | 71%                          |
| • Adjusted unemployment benefit | 14              | 52%                 | 82%                          |
| <b>2016</b>                     |                 |                     |                              |
| MS with IWB                     | 20              | 71%                 | 100%                         |
| • In-work cash transfers        | 5               | 18%                 | 25%                          |
| • Earned income tax credits     | 12              | 43%                 | 60%                          |
| • Adjusted unemployment benefit | 17              | 61%                 | 85%                          |

Source: Abbas, J. (2020), [What role for “in-work benefits”? A comparison of policies in EU Member States, 2006-2017](#), Ph.D. thesis, University of Bath, p.121.

Adjusted unemployment benefits and earned income tax credits were the main categories of IWB across the EU Members States in both points of time and adjusted employment benefit increased the most (by 9%) between 2008 and 2016.

In 2008, at least one of the three broad IWB sub-types were identified for the following countries: Ireland, the UK, Finland Sweden, Denmark, Austria, Belgium, France, Luxembourg, the Netherlands, Germany, Italy, Spain, Portugal, Greece, Hungary and Slovakia. For 2016, all of the same countries, but Hungary had IWB. Additionally, relevant policies were identified in Estonia, Slovenia and Malta. On the flipside, earned income tax credits, adjustable unemployment benefits and in-work cash transfers were not identified in Cyprus, Bulgaria, Czechia, Latvia, Lithuania, Poland and Romania for both time points. And were not in the following countries for one of the two time points: Malta (2008 only), Estonia (2008 only), Hungary (2016 only).

The number of Southern countries with IWB increased between 2008 and 2016: from two thirds to 87%, respectively. Malta did not have IWB in 2008, but it did by 2016. Cyprus was an outlier as the only country with no IWB for both time points. In even starker contrast, IWB were identified in just a fifth of CEE countries for 2008. Yet, like the Southern countries, there was an increase in the proportion of CEE countries with IWB by 2016. Slovenia and Estonia did not have IWB in 2008 but both had them in 2016. Croatia was not part of the EU in 2008, but IWB were identified in 2016. Slovakia is the exception as the only CEE country with IWB in both 2008 and 2016. Finally, Hungary is the only EU Member State where IWB were present in 2008 but not in 2016. For more details see Annex 1 (IWB in EU27/28 in 2008 and 2016).



## Classification of in work benefits and criteria of their efficiency

Most studies indicate that IWB result in positive effects at the extensive margins (the decision to work or not to work<sup>3</sup>). The evidence about the intensive margin (the decision on the number of hours worked) is more mixed<sup>4</sup>. In this respect the appropriate design of IWB is crucial to avoid the situation when many IWB beneficiaries work (very) limited working hours. The benefit should also encourage a progressive increase of the beneficiaries' working hours as they become more employable and productive through skills acquired during employment and work experience itself. Some Member States (Belgium and the Netherlands) a minimum threshold of hours worked is required (min. 15 hours/week. Others have decided to introduce the condition of full-time employment as the eligibility criterion (for example Ireland and the UK).

Another important factor is the balance between income and substitution effect as it influences individual's decisions to take up (or not) employment. What needs to be avoided is that an individual may reduce his/her working hours as in-work benefits increase disposable incomes and the same income level requires less effort. The substitution effect is related to the hourly wage and its combination with a possible top up resulting from minimum income: if one can gain more per hour worked, he/she will be encouraged to work more hours. Low-income workers are more responsive to financial incentives (the substitution effect) than the middle or high-income earners.

### *The efficiency criteria*

In order to ensure that IWB are efficient and bring positive employment results the following criteria should be met:

- **adequate targeting** on the groups that are most sensitive to changes in financial incentives<sup>5</sup>: primarily low-earners, including single parents with children and one-earner couples (with or without children), also older workers and low-skilled. Deciding on the right targeting is best done at an individual Member State's level taking into account the expected positive impacts in terms of employment growth and the related savings for public resources;
- **appropriate "entry" conditions**: the most common entry criterion is a requirement to be welfare recipient for a minimum one year to qualify for the IWB. Such requirements need to be considered carefully avoiding keeping people away from the labour market or demotivate them to look for a job. Another problematic "entry" condition is the level of individual wealth/earnings/family income as it carries the stigma effect as well as taking it into account may create disincentives to work longer hours or increase work effort;
- **appropriate interrelations between IWB and other benefits** are especially important to ensure equity. Available evidence shows that complete elimination of welfare benefits to increase financial incentives would ignore the complexity of

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<sup>3</sup> The most researched types of IWB are the Earned Income Tax Credit (EITC in the U.S.) and the Working Family Tax Credit (WFTC in the UK). In both cases positive employment effects on employment have been found. However, there are studies that argue that the EITC mainly encourages individuals to remain in employment, rather than increase the likelihood to take up a job.

<sup>4</sup> Vandelannoote, D., Verbist, G., (2017), *The impact of in-work benefits on employment and poverty*, Euromod Working Paper Series, EM 4/17, pp. 2-3

<sup>5</sup> It is worth noting that the level of benefits tends to be much lower in the countries where the schemes are available to a wide range of groups than in countries where the schemes are more targeted. Refundable tax-credits to all working individuals with low income are available in Belgium, Finland and France, but the maximum amount of benefit is rather small – below 2,6% of average earning.



diverse social needs. Consequently, striking the right balance between IWB and other benefits is a key;

- **well-defined rate of benefit withdrawal:** in case of more generous benefits, the withdrawal should be quicker, and in case of less generous schemes – lower benefit withdrawal rate is appropriate (i.e. 20% in the U.S.).

**Reflection point: benefit level and withdrawal rate**

OECD observes that: “(...) The issue of how large an in-work benefit should be and at what rate it should be withdrawn is crucial and at the same time very difficult to address. In-work benefits should be large enough to create a sizeable difference between welfare income and work income, but their optimal level would depend on factors such as levels of income support relative to wage rates of the less skilled, the minimum wage and the costs of working (which include transport, childcare, etc.). In addition, as governments tend to be budget constrained, the overall cost of the programme would influence the size of in-work benefits and the expected welfare gains. Overall, the optimal benefit levels and phasing-out rates have been shown to depend on where most of the labour supply effect is likely to come from: an increase in labour market participation versus an increase in hours worked. In this respect, Saez in his article titled “Optimal Income Transfers Programs: intensive versus extensive labour supply responses” published in 2002 showed that when most of the effect is observed in terms of labour market participation – i.e. going from non-employment to work – the optimal transfer programme should resemble the Earned Income Tax Credit of the United States, with a small guaranteed income and low benefit withdrawal rates. On the other hand, when most of the effect is expected to be in terms of changes in hours worked, rather than in participation decisions, the best choice would be a programme with high guaranteed income and a high phasing out rate. However, Saez’s model does not consider the additional cost of long-term unemployment, in terms of loss of skills. If this was introduced in the social welfare function, it would be likely to reinforce the superiority of programmes with relatively low guaranteed income and low withdrawal rates (...).”

Source: OECD (2005), *Increasing Financial Incentives to Work: The Role of In-Work Benefits*, OECD Employment Outlook, p.150.

- **appropriate level of IWB** should be high enough to create a meaningful difference between welfare income and work income. Their optimal level depends on such factors as the level of wages of the low-skilled workers, the minimum wage and the cost of enabling services (i.e. transport, childcare etc.). In general, a more targeted approach (and in this case usually more generous) helps a smaller number of people but tends to be more effective in encouraging the return to self-sufficiency.
- **appropriate time limits:** time limits in IWB remove disincentives to move up the wage ladder as well as limits the cost of the programme. It is very important to correctly define IWB time limits: for example, the evidence shows that IWB for the low-skilled available for a relatively limited time (6-12 months) do not lead to significant wage growth and may result in dropping of the labour market or moving to another welfare programme instead of contributing to long-term self-sufficiency. To ensure meaningful results, IWB recipients need to be supported in parallel by public or private employment services to help them develop their employability with a view to having access to full-time and stable employment opportunities.
- **working hours limits:** there are arguments that IWB should be limited to those working full-time to avoid the situation when beneficiaries choose part-time employment and “top up” their salary with IWB. However, such an approach may limit job opportunities for those on welfare who can work only part-time, i.e. mothers of

young children, single parents or young people continuing education<sup>6</sup>. Different IWB schemes may follow different approaches to this in view of the target groups realities and needs.

*Challenges related to IWB and possible solutions*

It is worth noting that **multiple programmes** are often addressed **to the same beneficiaries**. This results in additional administrative burden as well as may create confusion for the government and the beneficiaries alike. An interesting solution would be introducing a “single welfare office” that would establish the eligibility for different programmes and dispense benefits. For example, in the UK its child tax-credit is paid together with basic Working Family Tax Credit (WFTC) benefit, which improves the coordination among different components of the welfare system, promotes transparency in the marginal effective tax and simplifies claiming procedure.

The chosen **form of IWB** will have an impact on payment method and frequency as well as will define the necessary institutional setup. There are three main IWB types: earned income tax credits, social security reductions for employees and in-work cash transfers. Tax credits are perceived as effective and enabling to avoid the stigma of claiming IWB. They are paid through wage package, which is positive for a beneficiary (they are paid more often than one end of year payment) but adds more administrative burden on employers. Some of the earned tax credits are “refundable” (the US example), whereas others reduce tax liability but do not result in a transfer - from this perspective they can be regarded as “non-refundable”.

Table 2. Countries with refundable and non-refundable earned income tax

|             | <b>Refundable</b>  | <b>Non-refundable</b>  |
|-------------|--|--|
| <b>2008</b> | Austria, Belgium, France, Slovakia (4)                   | Ireland, Denmark, Finland, Italy, the Netherlands, Sweden (6)          |
| <b>2016</b> | Austria, Belgium, Luxembourg, Italy, Spain, Slovakia (6) | Ireland, the Netherlands, Denmark, Finland, Sweden, Italy, Estonia (7) |

Source: Abbas, J. (2020), [\*What role for “in-work benefits”? A comparison of policies in EU Member States, 2006-2017\*](#), Ph.D. thesis, University of Bath, p. 121.

It has already been stated that IWB must be considered with other benefits. A necessary **complement of any IWB is high-quality childcare**, essential component to raise women’s incentives to work. Childcare cost is a significant work-related cost for parents, especially single parents or second earners. Evidence shows that it is especially important for female workers as they are sensitive to effective wage - earnings net of childcare costs and childcare subsidies, rather than gross wage.

It is worth noting that some Member States offer “**activation prime**” - a special provision for individuals who start work after a period of unemployment or inactivity (usually in a form of a lump-sum). This is an interesting solution to increase attractiveness of IWB and their take up.

<sup>6</sup> To mitigate the effects of a full-time work requirement for this group of beneficiaries, introducing childcare cost subsidies would be an interesting policy option. For example, in the UK the Working Family Tax Credit (WFTC) is offered to parents with childcare responsibilities; at the same time a special bonus for those working full time is provided.



### **"Activation prime"**

The "activation prime" is available in eight out of the twelve Member States that have introduced some sort of IWB. These IWB are addressed to the long-term unemployed individuals only (Belgium, Ireland) or all individuals who find employment (the employment-conditioned benefit in the Netherlands). In Ireland "activation prime" is conditioned by transition for full-time employment; in Belgium and the Netherlands a minimum threshold of hours worked is required (min. 15 hours/week). Additionally, in Ireland and the Netherlands, two further payments of decreasing amounts are available for those who remain in employment in each of the two following years. Implementing such deferred payments should take into consideration the need to return to natural labour market dynamics and avoid keeping people in a subsidised employment if/when they become able to work and become self-sufficient without public financial support.

*Source: own elaboration on the basis of OECD (2005), *Increasing Financial Incentives to Work: The Role of In-Work Benefits*, OECD Employment Outlook, p.145.*

Finally, there are technical trade-offs that need to be considered while designing IWB. The key decision regards **a choice of the envisaged beneficiaries**: the family or an individual. The family-oriented provisions are better suited to redistribution, whereas individual provisions are better geared towards employment goals as they avoid the "adverse" effect on second earners. It is worth noting that in 2017 approx. 50% of the identified policies were only available for households with children. This indicates a special concern for children well-being and preventing their poverty, however, leaves aside individuals without children.

### **Employers' views: how to design effective in-work benefits?**

In-work-benefit scheme should aim at increasing employment participation - without raising the labour cost for employers - and, at the same time, combating in-work poverty. The reduction of social security contributions, especially for low paid employees, could contribute to achieving this target. The **in-work-benefit** must be provided **only to low-paid employees** and most promote full time employment.

While designing IWB, their **interaction with other redistributive and labour market measures needs to be taken into consideration**. IWB increase the gap between disposable incomes of those in work and those inactive. This is to some extent justified to make work an attractive option but needs to be balanced with social protection considerations, especially the solutions addressed to the most vulnerable in our societies. As a result, such policy aspects as levels and eligibility conditions of out-of-work benefits, tax burden on low-wage workers, regulations influencing wage levels and distribution (for example, statutory minimum wages) will also impact the functioning on in-work benefits.

Benefits should always provide **financial incentive for individuals to enter employment**. When designing in-work benefits it is therefore important to look at the difference between the level of total subsidies from the state (minimum income, unemployment benefits, housing subsidies etc.) and the minimum wage that you can expect through employment.

Any IWB scheme should be evidence based and that they have proven to have a positive effect on the employment. **New and pilot initiatives should be temporary** and should be evaluated using a control group. If in-work benefits should be used at a larger scale, it is essential that they have positive effects for employment and economy in general. Otherwise, there is a risk that they will create more harm than good.



*National approaches to designing IWB*

IWB implemented at the national level are mainly addressed to workers from vulnerable groups: these may be the workers from sectors with atypical working hours (Malta) or the unemployed immigrant workers (Sweden).

Malta: lump-sum for workers from sectors with atypical working hours

The Maltese Government had announced that as of 2022 it would introduce a new in-work benefit scheme worth 150 EUR/year for workers from the private sector with atypical working hours (in the evenings, on weekends and shifts)<sup>7</sup>. The scheme was to be addressed to workers from such sectors as accommodation, catering, administrative services and support, manufacturing, transport, storage and retail/wholesale. To qualify for the scheme the annual income should not exceed 20 000 EUR. Workers would be eligible for the benefit after having worked at least six months over a calendar year in one of the sectors. The scheme was to assist approx. 40 000 workers, with the benefit being equivalent to approx. 10% of the income tax that they pay. The total value of the benefit redistributed among these workers was to total at 6 mln EUR.

Sweden: entry job agreements to facilitate transition to open labour market

In Sweden, historically the unemployment has been high among those with low education and/or limited work experience. This situation is mainly caused by high minimum wages stipulated by collective agreements, rigid labour law and few jobs that require only low levels of education or work experience. As a response to the refugee crisis in 2015, the Swedish social partners signed a preliminary agreement in 2017 introducing a new scheme called "entry job agreements". The scheme is to be made operational over the course of 2022.

The "entry job agreements" will be designed on the basis of the national collective agreement, but must also be complemented with sectoral collective agreements. They are targeted at newly arrived immigrants (unemployed over 12 months) and the long-term unemployed (without work over 24 months). Temporary contract of a duration of maximum 24 months is signed with the aim to lead to an open-ended contract. Employer pays a fix amount of 8 400 SEK/month incl. social contributions. This corresponds on average to approx. 30 % of a regular minimum labour cost in collective agreements. The state provides - directly to the employee - a tax-free, individual state benefit. The amount will vary among sectors, it can be up to 9 870 SEK/month. Hence, the employee receives a net salary equivalent to minimum wage in the relevant collective agreement.

Additionally, relevant education and/or training, for instance language programmes, that is agreed upon by employer and employee will be provided. Private staffing and recruiting companies will be involved through public tender to provide support in order to achieve good matching. The political ambition is that the scheme provides work for 10 000 unemployed (the total number of the unemployed in Sweden in February 2022 was approx. 365 000).

Effective IWB schemes should be accompanied by the career support measures such as career guidance or better job matching (the Swedish example above). Training opportunities, notably up and re-skilling, are a very important component as they will be decisive for the transition to the open labour market and self-sufficiency. In some IWB schemes this component is missing (Italy).

<sup>7</sup> Despite the fact that the new IWB has been announced in [the Budget speech](#), it is still not officially introduced.



Italy: comprehensive IWB system, but missing upskilling/reskilling component

A comprehensive system of in-work benefits to promote access to the labour market for specific groups and those in the disadvantaged situations exists in Italy. Each year the Budget law updates and integrates different types of incentives, according to the specific national economic and social circumstances. Both the structural incentives and the ones adopted in the emergency context are compliant with the EU rules on state aid.

The system is quite complex and includes tax and social security contribution incentives for private employers hiring people from vulnerable groups. The incentives are aimed at promoting sustainable employment of young people (younger than 35 years old). Incentives also apply to different types of apprenticeships that are addressed to different age groups. The first apprenticeships are available for those aged 15-25, the professional ones to those aged 18-29 years of age and third level apprenticeships are available for those from the 18 to 29 years- age bracket). There are also incentives addressed to the unemployed workers aged over 50 years old, to workers hired with open-ended contracts, to the unemployed women and substitute workers who replace workers on leave as well as to the beneficiaries of the *Reddito di Cittadinanza* (the Italian minimum income scheme) and to beneficiaries of the unemployment benefit.

The Budget Law 2022 has provided additional incentives for private employers, to be applied also in relation to the economic crisis due to the Covid-19 pandemic. These incentives apply in case of hiring specific groups of workers: those who were employed in companies hit by the crisis, young people below 36 years old, people living in the most disadvantaged area of Italy /Southern Regions; workers suspended from work under *Cassa Integrazione* (short-time work schemes applied during crises).

*Confindustria's assessment*

Confindustria acknowledges the fact that IWB have a role in assisting companies and workers to overcome the effects of the economic crisis, certainly worsened by the Covid-19 pandemic. However, Confindustria has some doubts as to the structure of the general framework for incentives. It stresses the need to overcome such an approach by implementing a wider reform aimed at a structural reduction of labour costs, specifically referring to employers' contributions to social security system. Furthermore, Confindustria believes that any policy providing in-work incentives/benefits should be focused on those initiatives that are linked to training, upskilling and reskilling of workers. These training provisions are crucial to re-qualify work towards new skills (especially as regards apprenticeships and secondary vocational education). Confindustria warns that without a strong and effective link to the training/upskilling/reskilling of workers, any policy and measure adopted will be ineffective in the long term and will not result in increasing employment rate.

IWB can be designed in such a way that they allow to combine different benefits (Denmark), but can also be replaced by the state activation programs (Hungary) that seems to be less effective in supporting transition to the open labour market.

Denmark: job “bonus” subsidy and less deduction in benefits

Denmark used to offer a top-up of the salary for those long-term unemployed who take up work. Such a “bonus” creates an additional incentive to find a job and, at the same time, avoids lowering the unemployment benefit. Additionally, it enables gaining professional experience, therefore supports employability of the beneficiary. This scheme is “profitable” for the state only if it brings positive employment outcomes by targeting those who otherwise would not have found employment.

Denmark had two job “bonus” schemes (*obpræmieordninger*) in the period of 2011-2012 and 2012-2014. The 2011-2012 scheme was addressed to single parents, while the 2012-2014 scheme targeted the long-term unemployed on social benefits. An independent research and analysis centre operating under the Ministry of the Interior and Housing concluded that the schemes had no positive effect on the employment or the salary level.



The schemes implemented in the period 2017-2019 introduced top up of the salary to the long-term unemployed (receiving the unemployment benefit or entitled to minimum income). Those who had been unemployed for a longer period (in case of the beneficiaries of minimum income: 47 weeks of the past 52 weeks; in case of the beneficiaries of the unemployment benefit: 71 weeks of the past 78 weeks) could get a top up equivalent of 10% of their salary with a cap of 336 EUR/month for the maximum period of 18 months. The total maximum top up amounted to 6 048 EUR. This scheme has also not shown a significant effect on the employment for people receiving minimum income benefits during their unemployment. Even when the top up level was increased, there was no positive effect observed. However, there was a significant positive effect for the unemployed who received unemployment benefits (benefits for people who have contributed to an unemployment insurance fund).

Recently the Danish government has decided to re-introduce a temporary job subsidy. As of 1 January 2024, it will apply to people who have been unemployed and on the minimum income for at least one year during the last three years. The subsidy will amount to 672 EUR paid as a tax-free lump sum after six months in a continuous employment. This scheme expires in the middle of 2025.

In Denmark there is a historical lack of labour supply both in the private and public sector. Therefore, the objective of another IWB introduced in Denmark - less deductions in benefits – is to make employment financially attractive. One of the recommendations put forward in 2021 introduced a new model for deductions in benefits for the earned salary. It stipulates that people on the lowest minimum income would be able to earn 540 EUR or work eight hours a week in a low-income job without deductions in their minimum income. This recommendation still needs to be discussed at the political level in Denmark. Additionally, the Danish government has decided to discontinue deduction in the state pension (including early retirement benefits) due to additional income earned by the beneficiary or his/her spouse or cohabitant. This amendment will make employment more attractive for seniors and pensioners. The amendment is expected to enter into force on 1 January 2023.

Hungary: public works scheme instead of employment incentives

Since 2010 the unemployment benefit in Hungary is paid only for three months and is decreasing (it equals 90% of the former salary in the first month, then drops to 80-70%). The public works scheme, introduced in 2008, is a wide-spread practice regardless of the individual's former employment history, qualifications or social situation. The public work scheme is organised by the municipalities and is not connected to the open labour market.

It is worth noting that recently the government has introduced the subsidies for workers who manage to find employment in the private sector. Additionally, different “pro-employment” incentives exist in Hungary: reimbursement of travel costs during job-seeking, benefits for the promotion of mobility, etc.

*BusinessHungary's assessment*

BusinessHungary stresses that the public work scheme does not create a link with the open labour market and by “trapping” people in the scheme, especially those with low-skills or in rural areas, does not facilitate their (re-) entry to the “real” labour market. BusinessHungary also stresses that the scheme lacks training component to align skills of the beneficiary with the labour market needs. This component would be especially important in the situation of growing labour shortages and skills mismatches. BusinessHungary believes that financial incentives are important but need to be accompanied with appropriate training provisions organised and delivered in strong cooperation of all the concerned actors: municipalities, public employment services and social partners.



Designing effective IWB should not only take into consideration other benefits to which potential beneficiaries are entitled, but also their assets (Germany).

Germany: means-tested IWB should support return to self-sufficiency

In Germany, under certain circumstances, it is possible for the employed persons to supplement their salary with additional funds. While being employed, these persons receive an additional amount of money within the structures of *Arbeitslosengeld II (ALG II)*, the lowest-level unemployment benefit). *ALG II* can be requested in addition to the salary in cases when the salary is insufficient to cover personal costs of living or the costs of living of the particular “community of need” (*Bedarfsgemeinschaft*, e. g. a family). Persons who are subject to this kind of scheme do not receive the full amount of *ALG II* they would receive if they were unemployed – only a so-called “supplementary amount” is granted. This amount is calculated taking into account the needs of the person or its “community of need” and the existing income (see Annex 1 for a simulation of the “supplementary amount” calculation).

The underlying principle for this benefit is “the encouragement principle”: the more an individual earns, the higher the difference is between his/her overall income and the amount he/she would receive while being unemployed. The eligibility criteria to qualify for the *ALG II* scheme include: being “in need of help” (assets such as real estate assets or a stock portfolio need to be liquidated; the concept of *Schonvermögen* - “sheltered assets” - applies), “priority benefits” (child allowance, parental allowance, child support payments, pensions) must be considered first and will be incorporated into calculating the “income” side of the equation.

*BDA’s assessment*

*ALG II* is also called “basic income/basic security” and shall provide a living wage for all those who cannot cover their most basic expenses. It is therefore good that also employed persons have access to *ALG II* funds in cases where their salary is not sufficient to fulfil basic needs. However, eligibility should exclusively apply to these persons and not be watered down/extended. The principle of “encouraging and challenging” needs to remain the priority, meaning that individuals should always be incentivised to be self-sufficient. *ALG II* in its function as an IWB shall therefore fulfil a bridging-aid function back to full-fledged employment with a salary that covers individual’s living expenses.

**Recommendations**

- It is crucial to ensure that **social investments and in-work benefits** are designed in a way that **underpins economic growth and employment participation** of benefit recipients.
- IWB are an interesting option in the current context of the strained public budgets and significant labour shortages. They are **politically more acceptable** than a rise in social benefits and more “employment friendly”. They are also seen as **more effective than increasing the minimum wage**, which might push up wage rates above the market equilibrium.
- Well-designed IWB are likely to be **more effective if paired with targeted active labour market policies** (ALMPs) as well as high-quality subsidized childcare provisions crucial for parents, and even more so for female workers.
- The Commission should take the opportunity of its **upcoming proposal for a Council recommendation on minimum income** to encourage Member States to put in place well-designed IWB schemes.



- As **part of their recovery and resilience plans**, national governments should investigate the role of **well-targeted and balanced in-work benefits** paid via social protection systems aiming to encourage employment participation and, at the same time, a reduction of in-work poverty. The related measures should appropriately balance the necessary focus on employment creation and participation, paying attention to income effects for low-skilled workers', the unemployed and the inactive. A key policy consideration, at a time when our economies are deeply tested, is to proceed with such measures without raising the cost of work for employers.
- The business community calls on the European Commission and on the Council's Employment and Social Protection Committees to prioritise policy learning and exchanges with social partners on in-work benefits to support Member States designing and implementing their policy initiatives in that field drawing on most effective existing in-work benefit schemes. The new tripartite Advisory Committee on Social Protection would be well-suited as a platform for this kind of exchanges.

In conclusion, in the current context of shrinking working age population, serious labour shortages across the EU labour markets, relatively high inactivity rate and public budgets under pressure, in-work benefits are a very interesting policy option. If well-designed, they have a potential to increase employment by helping those from vulnerable groups to access or return to the labour market.

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**Annex 1. IWB in EU27/28 in 2008 and 2016**

| Regime             | Country | Policies identified |             | In-work cash transfers |             | Earned income tax credits |             | Adjusted unemployment benefits |             |
|--------------------|---------|---------------------|-------------|------------------------|-------------|---------------------------|-------------|--------------------------------|-------------|
|                    |         | 2008                | 2016        | 2008                   | 2016        | 2008                      | 2016        | 2008                           | 2016        |
| <b>Years:</b>      |         | 2008                | 2016        | 2008                   | 2016        | 2008                      | 2016        | 2008                           | 2016        |
| <b>Liberal</b>     | IE      | ✓                   | ✓           | ✓                      | ✓           | ✓                         | ✓           | ✓                              | ✓           |
|                    | UK      | ✓                   | ✓           | ✓                      | ✓           |                           |             | ✓                              | ✓           |
| Regime total (%)   |         | 2<br>(100%)         | 2<br>(100%) | 2<br>(100%)            | 2<br>(100%) | 1<br>(50%)                | 1<br>(50%)  | 2<br>(100%)                    | 2<br>(100%) |
| <b>Nordic</b>      | FI      | ✓                   | ✓           |                        |             | ✓                         | ✓           | ✓                              | ✓           |
|                    | SE      | ✓                   | ✓           |                        |             | ✓                         | ✓           | ✓                              | ✓           |
|                    | DK      | ✓                   | ✓           |                        |             | ✓                         | ✓           | ✓                              | ✓           |
| Regime total (%)   |         | 3<br>(100%)         | 3<br>(100%) | 0                      | 0           | 3<br>(100%)               | 3<br>(100%) | 3<br>(100%)                    | 3<br>(100%) |
| <b>Bismarckian</b> | AT      | ✓                   | ✓           |                        |             | ✓                         | ✓           | ✓                              | ✓           |
|                    | BE      | ✓                   | ✓           |                        |             | ✓                         | ✓           | ✓                              | ✓           |
|                    | FR      | ✓                   | ✓           |                        | ✓           | ✓                         |             | ✓                              | ✓           |
|                    | LU      | ✓                   | ✓           |                        |             |                           | ✓           | ✓                              | ✓           |
|                    | NL      | ✓                   | ✓           |                        |             | ✓                         | ✓           | ✓                              | ✓           |
|                    | DE      | ✓                   | ✓           |                        |             |                           |             | ✓                              | ✓           |
| Regime total (%)   |         | 6<br>(100%)         | 6<br>(100%) | 0                      | 1<br>(17%)  | 4<br>(67%)                | 4<br>(67%)  | 6<br>(100%)                    | 6<br>(100%) |
| <b>Southern</b>    | IT      | ✓                   | ✓           | ✓                      | ✓           | ✓                         | ✓           |                                |             |
|                    | MT      |                     | ✓           |                        | ✓           |                           |             |                                | ✓           |
|                    | ES      | ✓                   | ✓           |                        |             | ✓                         | ✓           | ✓                              | ✓           |
|                    | PT      | ✓                   | ✓           |                        |             |                           |             | ✓                              | ✓           |
|                    | EL      | ✓                   | ✓           |                        |             |                           |             | ✓                              | ✓           |
|                    | CY      |                     |             |                        |             |                           |             |                                |             |
| Regime total (%)   |         | 4<br>(67%)          | 5<br>(83%)  | 1<br>(17%)             | 2<br>(33%)  | 2<br>(33%)                | 2<br>(33%)  | 3<br>(50%)                     | 4<br>(67%)  |
| <b>CEEC</b>        | BG      |                     |             |                        |             |                           |             |                                |             |
|                    | HR      | na                  | ✓           | na                     |             | na                        |             | na                             | ✓           |
|                    | CZ      |                     |             |                        |             |                           |             |                                |             |
|                    | EE      |                     | ✓           |                        |             |                           |             |                                |             |
|                    | HU      | ✓                   |             |                        |             |                           |             |                                |             |
|                    | LV      |                     |             |                        |             |                           |             |                                |             |
|                    | LT      |                     |             |                        |             |                           |             |                                |             |
|                    | PL      |                     |             |                        |             |                           |             |                                |             |
|                    | RO      |                     |             |                        |             |                           |             |                                |             |
|                    | SK      | ✓                   | ✓           |                        |             |                           |             |                                |             |
| SI                 |         | ✓                   |             |                        |             |                           |             |                                |             |
| Regime total (%)   |         | 2<br>(20%)          | 4<br>(36%)  | 0                      | 0           | 2<br>(20%)                | 2<br>(18%)  | 0                              | 2<br>(18%)  |

Source: Abbas, J. (2020), [What role for "in-work benefits"? A comparison of policies in EU Member States, 2006-2017](#), Ph.D. thesis, University of Bath, p. 123.

**Annex 2.**

Germany: a calculation of the “supplementary amount”

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- **Example for Person X**

- Single, no children
- 35 yrs old
- Rent (costs of accommodation and heating): 410 EUR
- Works 10 hrs/week
- Gross monthly income: 650 EUR
- Net monthly income: 553,50 EUR
- Allowance lump sum (calculated based on gross monthly income): 210 EUR
- *ALG II* lump sum for regular needs (*Regelbedarf*) for singles: 449 EUR

| NEED   |            |                           |                            |
|--|------------|---------------------------|----------------------------|
| Lump sum regular need ( <i>Regelbedarf</i> ) for singles |            | 449,00 EUR                |                            |
| Accommodation  |            | 410,00 EUR                |                            |
| <b>OVERALL NEED</b>                                      |            | <b>859,00 EUR (sum A)</b> |                            |
| INCOME   |            |                           |                            |
| Net income   |            | 553,50 EUR                |                            |
| Allowance  |            | - 210,00 EUR              |                            |
| <b>INCOME TO BE TAKEN INTO ACCOUNT</b>                   |            | <b>343,50 EUR</b>         |                            |
| <b>ELIGIBILITY / CLAIM (supplementary amount)</b>        | 859,00 EUR | - 343,50 EUR              | <b>515,50 EUR</b>          |
| <b>Overall amount received</b>                           | 553,50 EUR | 515,50 EUR                | <b>1.069,- EUR (sum B)</b> |

- Person X receives a supplementary sum of 515,50 EUR
  - Added to the monthly net salary of 553,50 EUR, Person X receives 1 069 EUR
  - If being unemployed and receiving only *ALG II*, Person X would receive the amount listed under “NEED” of 859 EUR
- ➔ By working and additionally receiving the supplementary amount, Person X’s monthly overall income is 210 EUR higher compared to the income Person X would receive when being unemployed

- **Note:**

- Sum A:  
the amount Person X would receive if being unemployed
  - Sum B:  
the (net) income (paid by the employer) + the supplementary amount (paid from state funds by the Federal Labour Agency)
- ➔ By rule, the allowance lump sum always equals sum B – sum A

Source: BDA (2022).