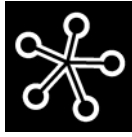


*University of Amsterdam*



**AMSTERDAM INSTITUTE FOR  
ADVANCED LABOUR STUDIES**

# **DISTRIBUTION OF RESPONSIBILITY FOR SOCIAL SECURITY AND LABOUR MARKET POLICY**

**COUNTRY REPORT: DENMARK**

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## **ABSTRACT**

High levels of unemployment, or high levels of social expenditures as well as the growing demand for a flexible labour force have given new impetus to the world-wide discussion on what model to use for an efficiently operating labour market and in particular on the role of institutions. Although there seems to be a growing consensus on the restricted governmental role in recent decades, this has not been translated into a unanimous appraisal of the role of intermediary organisations, such as trade unions. There is no clear view on an appropriate distribution of responsibility between government, social partners and the market. The research project 'distribution of responsibility for social security' aims to create a scientific basis for a clear and consistent view on the role and distribution of responsibilities between the different labour market institutions. As part of this research project, this paper provides an elaborate country study of Denmark.

It is shown that legislation of unemployment insurance and active labour market policy is set by the national government. Legislation with respect to employment protection, however, is largely left to the social partners, i.e. the dismissal of salaried workers is regulated by a special piece of national law, while the rules for blue-collar workers are defined as part of the negotiations between the social partners. The Danish system of unemployment insurance and active labour market policy is a two-tier system: unemployment insurance for members of unemployment insurance funds and social assistance for non-members. The first tier is basically state-run system, while the second tier is administered by the municipalities. As for the performance of the Danish labour market, participation rates are quite high and although unemployment rates are relatively high and differentiated across groups, this is dominated by short-term unemployment.



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## **I INTRODUCTION**

### **I.1 A QUICK VIEW ON EMPLOYMENT PROTECTION, SOCIAL INSURANCE AND LABOUR MARKET POLICY**

#### **I.1.1 EMPLOYMENT PROTECTION**

In the recent exposure given to the Danish employment system (often labelled the Danish “flexicurity-model”), it is generally emphasised that the overall level of employment protection in Denmark is at a low level and comparable to liberal labour markets like that of the United Kingdom. Furthermore, this low level of protection is a long-standing feature of the Danish labour market dating back to the General Agreement between the social partners that was the outcome of a general strike in 1899. The so-called September-agreement defined the right for the employers to manage the work-place (including the right to hire and dismiss workers), while the employers on the other hand recognised the trade unions as legitimate counterparts in negotiations about wages and work conditions. One of the characteristics of the Danish labour market, which is in contrast to for instance the situation in Sweden, is that this low level of employment protection has been intact until present times.

Regulating individual employment protection and setting rules concerning dismissals is therefore left to the social partners. As a result of this, a closer look at the employment protection found on the Danish labour market will reveal that the level of protection against dismissals varies between different groups and between different sectors. By example, in the construction sector dismissal periods can be only one day, while other blue-collar workers have an employment protection similar to that of salaried workers (*cf.* below). The wide dispersion between the different groups of employees when it comes to employment protection legislation makes it difficult to use the OECD-method of aggregating the different rules to a single number indicating the EPL-strictness for the labour market as a whole. Nevertheless, the overall assessment of employment protection in Denmark is however that the protection level is in the lower end of the spectrum, *cf.* Figure I.1.<sup>1</sup>

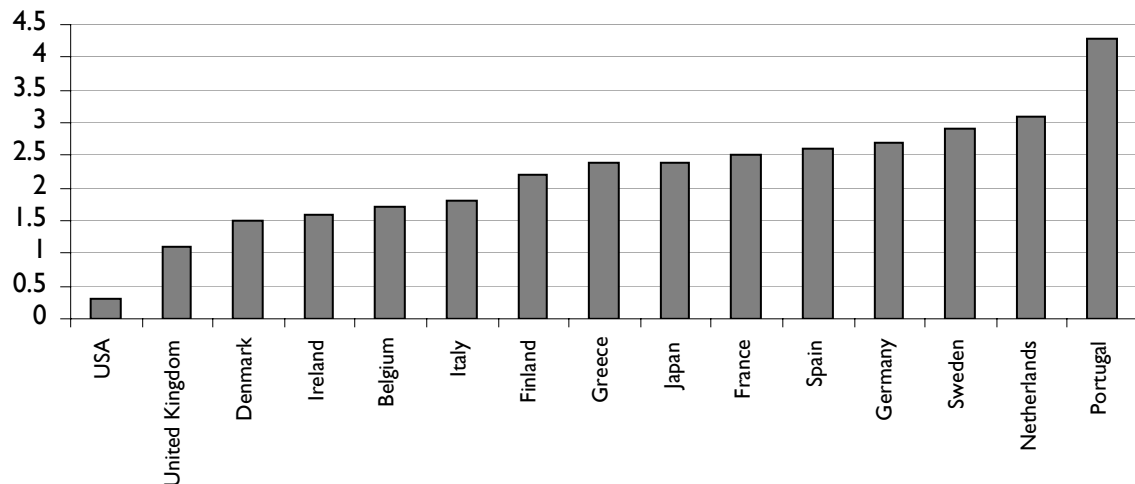
As an important exception, the dismissal of salaried workers is regulated by a special piece of legislation, while the rules for blue-collar workers, as mentioned, are defined as part of the general negotiations between the social partners. But even for salaried workers the term of notice is rather short, depending however on the seniority of the employee. For a seniority of less than three years, the notice period is three months. The maximum notice period is 6 months after at least 9 years of

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<sup>1</sup> In Section 2.2 a closer look is taken at the employment protection for different groups.

employment. For some groups the employer also must present a concrete reason for the dismissal, either based on circumstances related to the employee or the firm.

Figure 1.1: OECD Employment protection index for ordinary employees with a permanent contract.



Source: OECD (2004b), chapter 2, Table 2.A2.1.

An interesting trait is that there are no special regulations for public employees, who are in general subject to the same rules as in the private sector. The exemption is the minority of public employees, who still have a special status as public servants, although the tendency over the last decades has been to phase out this category of public employees.

### 1.1.2 SOCIAL INSURANCE

A characteristic feature of Danish social security and labour market policy is the development and stability of a two-tier system – one for the employed and unemployed – and one for those groups with no attachment to the labour market (Damgaard, 2003). Until the end of the 1800-years both systems had social security as their focus. The municipalities were in charge of a public system that took care of those in need, while the guilds supported sickness insurance for the craftsmen and provided work for the unemployed members. Over the last hundred years those two systems grew into the present day two-tier system.

The Danish system of unemployment insurance is based on the so-called Ghent-system. It consists of 31 state recognised unemployment insurance funds. Ten of them operate within specific occupational fields, which means that only employed persons from specific occupational fields can become members. Thirteen of the unemployment insurance funds operate within specific occupational fields, but also admit self-employed persons working within the occupational field as members. Three of them are cross-occupational unemployment funds, which mean that they admit

employed persons from all occupational fields as members. Four of them are unemployment funds for both employed persons and self-employed persons. One unemployment insurance fund only admits self-employed persons as members. When a person moves from one unemployment fund to another, either due to a shift in occupation or because s/he decides to do so, the right to unemployment benefits are transferred at the same time.

Most of the unemployment insurance funds are affiliated with one or more trade unions. While membership of an unemployment insurance fund is independent of being a member of a trade union, most workers will conceive the membership of the trade union and the affiliated unemployment insurance fund as a package. This is probably due to the long historical bonds between the two institutions and to the fact that trade unions do little to advertise the formal difference between the two kinds of membership. Also, of course, membership of a trade union offers some advantages, which are unrelated to receiving unemployment benefits like support in wage negotiations and conflicts with the employer.

The present version of the system for economic support for the unemployed dates back to the last large reform of the unemployment benefit system in 1969, where the state took over the responsibility for financing the extra costs of unemployment benefits that were caused by increases in unemployment (the principle of public financing “at the margin”). The members of the unemployment insurance funds will therefore only be obliged to pay a fixed membership contribution, independent of the actual level of unemployment. This mechanism for financing unemployment insurance implies that the share of public funding depends on the total number of unemployed. In periods of high unemployment as in the early 1990s, the Government’s share rises to 80 percent, while it falls to less than 50 percent during economic upswings.

Apart from those having exhausted their right to unemployment benefits, the group of “non-insured” unemployed consist of those unemployed, which do not fulfil the criteria for becoming eligible to unemployment benefits in the first place (*cf.* the list of criteria presented below). The group of unemployed must apply for cash-benefits administered by the local government (the municipalities). Cash benefits are means-tested and the amount depends on the family-situation of the unemployed.

### **1.1.3 ACTIVE LABOUR MARKET POLICY**

Until the end of 2006, the basic Danish system of labour market policy is organised around three levels: the state level, the regional level and the municipalities. The regional level is made up by of 14

regions (counties), excluding the large municipalities of Copenhagen and Frederiksberg that have a special status within the regional level. The local level is structured around 271 municipalities (including the municipalities of Copenhagen and Frederiksberg).

In broad terms the division of labour between the regional level and the local level is that the regions are responsible for health care and secondary education, while most other public services (including primary schools, social services and care for the elderly) are delivered by the municipalities. As already noted, due to their right to collect their own taxes, regional and local government share a rather high level of independence.

When assessing the degree of decentralisation, one should add however that the activities of the regions and municipalities are regulated by a number of laws and other regulations set at the central level, for instance with respect to standards for primary schools, obligations towards unemployed recipients of social benefits etc. The balance between allocation of responsibilities, control and financing is the core theme of the yearly negotiations between the Government and the organisations of the regions and the municipalities.

Labour market policy and the Public Employment Service [*Arbejdsformidlingen*] have a special status, being the responsibility of the central government, but implemented by special bodies (Regional Labour Market Councils and labour offices) at the regional level. These institutions are not part of the structure of regional government, but belong to the central government.

The Regional Labour Market Councils [*Regionale Arbejdsmarkedsråd*] are tripartite bodies with representatives both from trade unions, employers organisations, regional and local government. These councils are responsible for the management of regional labour market policy initiatives within the framework laid down at the central level. The system is based on a management-by-objectives approach. Thus, the Regional Labour Market Councils receive a lump-sum for active measures and have a large discretion with respect to the actual allocation of funds between different programmes – typically in cooperation with public actors (e.g. educational institutions) or private actors (e.g. private training providers). Therefore, the Regional Labour Market Councils are important partners in local employment development.

At the national level, a National Labour Market Council [*Landsarbejdsrådet*] has been set up with a similar composition. This Council acts in an advisory capacity to the Minister of Employment concerning, *inter alia*, such matters as the planning of labour market initiatives and the laying down of the framework for measures at the regional level.

#### **1.1.4 INDUSTRIAL RELATIONS**

Out of the total Danish number of wage earners of 2,656 million persons, 2,120 million persons were members of a trade union in 2004, giving a rate of organisation of about 80 percent. Of the organised workers, about two-thirds are members of the Danish Confederation of Trade Unions (LO), while the remainder are members of various white-collar unions. In a detailed study of union membership from 2000, the rate of unionisation in the public sector is reported as very high (around 90 percent), while the rate in the private sector is 77 percent (Madsen, 2000). The rate is slight higher for women than for men (83 percent versus 80 percent) and significantly lower for those aged less than 30 years (69 percent versus 85 percent for the older workers). The unionisation rate is highest for skilled workers and employees with a short or medium cycle education.

After two decades of increase, the membership of many trade unions, including Danish Confederation of Trade Unions (LO) has stagnated or declined in recent years – although it is still very high by international standards. Several reasons have been promoted for this development (Madsen, 2000):

- A demographic effect with a lower propensity of younger cohorts to become members of a trade union;
- Changing structure of employment by sectors and jobs-levels can have a negative influence on membership of those unions that recruit blue-collar workers from traditional industrial sectors; and
- Rising costs of membership; one cause is that the tax rebate has been lowered. The membership contribution is still deducted from taxable income, but the reduction in taxes is always calculated for the lowest level of marginal tax rates, not the for the marginal tax rate of the person's actual income level, as was the previous rule.

The principle of the “closed shop”, which until recently was a rule for about 10 percent of Danish wage earners, has now been declared illegal. Membership of a trade union is therefore voluntary, but in many work places there will be a strong social pressure of the employees to become members. Furthermore, the de-central character of wage bargaining and the strong role of shop stewards in the bargaining process probably acts as strong incentives for members, as does the close relation between the trade unions and the unemployment insurance funds.

The share of wage earners covered by collective agreements is 100 percent in the public sector and 77 percent in the private sector (Dansk Arbejdsgiverforening, 2005: Table 6.1). .

## **1.2 RELATION BETWEEN UNEMPLOYMENT INSURANCE, EMPLOYMENT PROTECTION AND LABOUR MARKET POLICY**

The balance and interplay between unemployment insurance, employment protection and ALMP are often summed up as being the main characteristics of the Danish flexicurity model in the following configuration:

- A flexible labour market with a high level of external numerical flexibility indicated by high levels of worker flows in and out of employment and unemployment;
- A low level of employment protection, allowing employers to adapt the workforce to changing economic conditions, makes the high degree of numerical flexibility possible;
- A generous system of economic support for the unemployed; and
- Active labour market policies aimed at upgrading the skills of those unemployed, that are unable to return directly from unemployment to a new job.

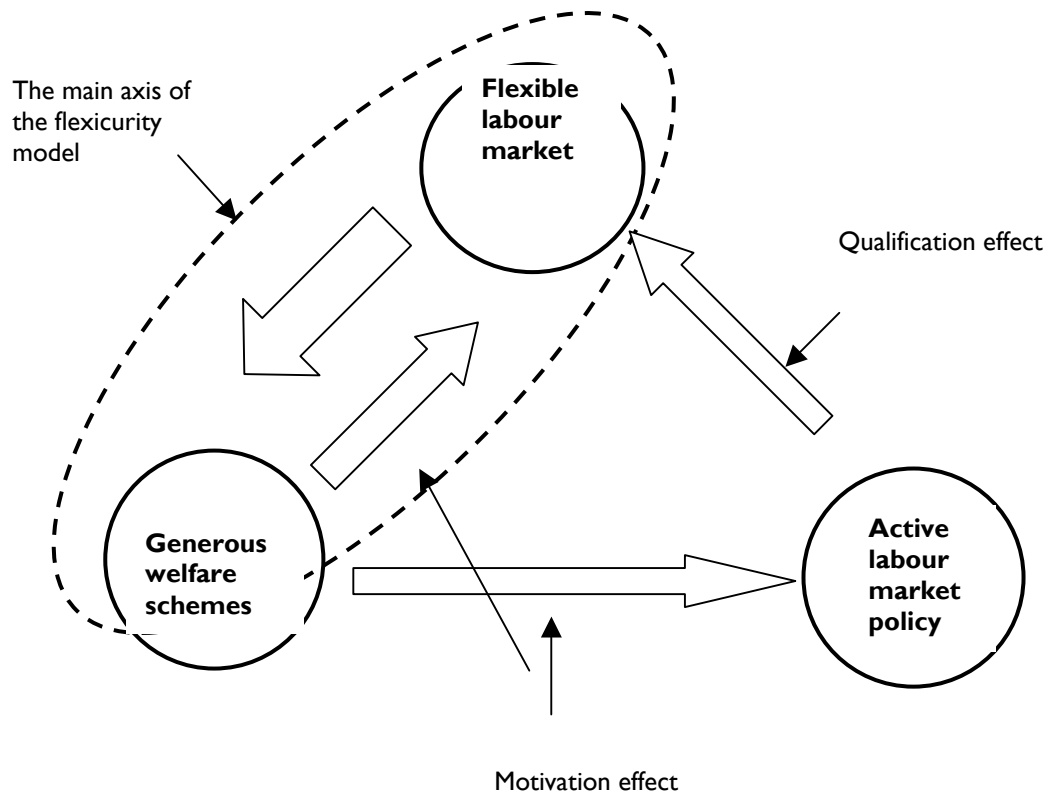
It is important to emphasise that while the term “flexicurity” has only recently been associated with the Danish employment system, its basic characteristics have a long history. Thus while the current attention paid to the Danish model is caused by the significant reduction in unemployment since 1993 and the high employment rate, one should not confuse this recent success with the creation of a fundamentally new version of the Danish employment system during the last decade. To the contrary one of the fascinating elements of the story about the Danish labour market is the fact that the model has been able to survive since the founding of the modern Danish welfare state in the 1960s in spite of the economic turmoil of the 1970s and 1980s. Furthermore it has been successful in supporting the ongoing structural changes in the economy, which has kept Denmark in a position among the most affluent countries in the world.

The Danish labour market model is often described as a ‘golden triangle’, cf. Figure 1.2. The model combines high mobility between jobs with a comprehensive social safety net for the unemployed and an active labour market policy. In fact the mobility (measured by job mobility, job creation, job destruction and average tenure) is remarkably high in an international comparison (Bingley *et al.*, 2000; Madsen, 2006). The high degree of mobility from employer to employer is definitely linked to the relatively modest level of job protection in the Danish labour market. Another reason could also be higher risk willingness among workers due to the comprehensive social safety net and probably also the low stigmatising effects of social security in Denmark.

Despite one of the lowest levels of job protection among OECD-countries (OECD, 2004b: chapter 2), Danish workers have a feeling of high job security among all subgroups of workers (Auer &

Casez, 2003). Also a recent Eurobarometer reported that a majority of more than 70 percent of the Danes found it a good thing to change jobs every few years.<sup>2</sup>

Figure 1.2: The Danish flexicurity model



Source: Madsen (2006).

The arrows between the corners of the triangle illustrate flows of people. Even if the unemployment rate is low in an international perspective (5.4 percent in 2004), Denmark almost has a European record in the percentage of employed which are each year affected by unemployment and receive unemployment benefits or social assistance (around 20 percent). But the majority of these unemployed persons manage to find their own way back into a new job. As an indication, the incidence of long-term unemployment as a percentage of total unemployment (6+ months, 12+ months) was in 2004 respectively 45 percent and 22.6 percent in Denmark compared to 60.4 percent and 42.4 percent in EU(15). Those who become long-term unemployed end up in the target group for the active labour market policy, which – ideally – helps them to find employment again. The model illustrates two of the most important effects in this connection. On the one hand, as a result of the active measures, the participants in various programmes (e.g. job training and education) are upgraded and therefore improve their chances of getting a job. This is the “qualification effect” of ALMP.

<sup>2</sup> See Eurobarometer Survey on Europeans and Mobility, 2006 ([http://ec.europa.eu/employment\\_social/workersmobility\\_2006/uploaded\\_files/documents/FIRST%20RESULTS\\_Web%20version\\_06.02.06.pdf](http://ec.europa.eu/employment_social/workersmobility_2006/uploaded_files/documents/FIRST%20RESULTS_Web%20version_06.02.06.pdf))

On the other hand, the measures can have a motivational (or threat) effect in that unemployed persons, who are approaching the time, when they are due for activation, may intensify their search for ordinary jobs, in case they consider activation a negative prospect. Thus one effect of labour market policy will be to influence the flow from unemployment benefits back to work, also for those unemployed, who do not actually participate in the active measures. A recent study has in fact argued that this motivational effect accounts for the major part of the macro-effect of ALMP (Rosholm & Svarer, 2004).

The social safety net in the shape of unemployment benefit and social assistance for the unemployed together with the high flexibility form the main axis of the model, in the sense that both elements have been characteristic of the Danish labour market for many years. Recognition of the employers' right to hire and fire at will date back to the September Compromise of 1899. Danish labour market parties here entered into an agreement that focused on labour market disputes and how to solve them, as well as the appropriate role of organisations in the system. This established centralised negotiations and mechanisms for resolving disputes also laid the foundation for the practice of self-regulation by labour market parties in most matters of importance to the labour market.

As described in more detail below, the Danish unemployment benefit system is based on the Ghent-system. It has its roots in the early 1900s, and in its present form dates back to the late 1960s. A generous (by international standards) and primarily government-financed benefit support system was established in 1969 and fairly wide frames for support were adopted. Unemployment benefits and the state's role in financing them were increased, eligibility requirements for insurance and unemployment benefits were reduced, and high levels of compensation for lost income were secured. In return, employers were exempted from compensating redundant employees, as this responsibility was taken over by the state. Consequently, employers have never had to secure employment and pay for redundancies, and the hiring and firing costs of Danish businesses have remained very low. On the other hand, the active labour market policy stressing upgrading of skills and job training is relatively new. In its present form, it originates from the labour market reform of 1993-94 and subsequent initiatives (Madsen, 2006).

The Danish development of the welfare state and labour market points towards an interesting hybrid between the flexible, liberal welfare states characterised by high numerical flexibility (liberal hiring-and-firing rules) and the generous Scandinavian welfare regimes of high benefit levels. The hybrid model manages to reconcile the dynamic forces of the free market economy with the social security of the Scandinavian welfare states. Some writers may be inclined to call this hybrid unstable and bound to eventually head off in one or the other of the two directions (Hall & Soskice, 2001).

However, when we have outlined the historical-institutional conditions behind the Danish flexicurity model below, it should be evident that this model is a result of a long evolutionary development, and is supported by relatively stable institutions and class compromises.

Both in the international as well as in the Danish debate there has, from time to time, been a tendency to jump to the conclusion that the success of the last decade is a result of the flexicurity model just described. It is, however, essential to point out that the positive development in the Danish labour market since the early 1990s is not attributable exclusively to the Danish flexicurity model. Without a successful balancing of the macroeconomic policy and the trends in the international business cycle, the growth in employment and the falling unemployment would not have been possible. The coinciding of low inflation and a halving of registered unemployment rates is also a by-product of a new agenda for collective bargaining and wage formation, which helped the labour market adjust to the shift from high unemployment to full employment while keeping wage increases at a moderate level and not departing from the international trend towards low inflation. This agenda developed gradually during the 1980s and was formalised by a joint declaration of the social partners in 1987, where they stated that they would take the international competitiveness and macro-economic balance of the Danish economy into account during wage-negotiations.

Table 1.1 sums up the main traits of the Danish system and its specific development in the 1990s.

### **1.3 A SHORT HISTORICAL OVERVIEW**

This section provides a brief historical overview of the development of the Danish system of social protection and labour market policy.

#### **1.3.1 SOCIAL SECURITY<sup>3</sup>**

Until the end of the 19th century social policy measures were virtually synonymous with poor relief, and only in the 1708 Poor Relief Act did help to the poor assume a relatively organised form; before this, the help offered consisted mainly of building poorhouses for those incapable of work and giving the poor permission to beg in their own parish. The Poor Relief Act of 1708 meant that each individual parish was given the responsibility of ensuring food, etc. for the poor of the parish who were incapable of work. The poor who were capable of work were sent to forced labour in, for instance, workhouses.

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<sup>3</sup> This section is based on excerpts from "Chapter 3: The conditions of life" published by the Danish Ministry of Foreign Affairs ([www.um.dk](http://www.um.dk))

Table 1.1: An overview of the Danish system of “flexicurity”

	Basic traits of the Danish system of “flexicurity”	Specific developments in the 1990s
Political environment	Strong corporatist structures Implicit social contract concerning balance between security and flexibility	Broad political support for reforms of labour market policies Acceptance by social partners of need for wage restraint Decentralization of wage formation
Macroeconomic environment	Changing international economic conditions Active fiscal policy, but constrained by external balance	Strong internal demand Favourable external balance Lower level of international inflation
Employment situation	High employment rate (around 75 percent) Shifting levels of open unemployment Rising share of persons receiving transfer income	Significant reduction in both open and gross unemployment Reduction in structural unemployment
Worker mobility (external numerical flexibility)	High by international standards	High by international standards
Employment protection	Weak	Weak
Unemployment benefits	Significant increase in compensation rate with reform in the late 1960s Cash benefits for non-insured unemployed	Slow decline in compensation rate, but still high by international standards Reduction in the maximum duration of unemployment benefits from 7 to 4 years
Active labour market policy	High expenditures on LMP in general Incremental policy adjustments since 1979	Decentralised Individualised Right and duty to early activation

Source: Madsen (2006), Table 1

In 1803 a tax was introduced to cover parishes' expenditure on poor relief. Recipients of poor relief had, after the introduction of a free constitution in 1849 no right to vote, and neither were they permitted to marry. An act of 1856 established the Fund for the Poor, which relied entirely on private donations, e.g. from church collection boxes; the Fund was aimed at giving relief before the poor were obliged to resort to the general system of poor relief and thereby lose their civil rights.

In 1891 the Act on Support in Old Age was passed, together with a revised Law on Poor Relief; this ensured, for instance, public aid for medical care, midwifery services and burial. The introduction of support in old age was epoch-making. All those above 60 years of age and in need for social assistance were given the status of deserving poor, i.e. they were given relief without losing their right to vote, a break with the previous practice governing poor relief, which smacked of alms giving. In addition, it was no longer only the parishes that bore the financial burden, but the State now also made its contribution.

In 1892 an Act on Health Insurance Societies was passed, encompassing a private, voluntary insurance principle with payment of contributions, but with a state subsidy. The idea of sickness benefit institutions built on a number of older, completely private health insurance societies, which provided members with various kinds of help during illness. Just prior to the passing of the Health Insurance Act, there were around 1,000 private health insurance societies with altogether over 100,000 members.

Similarly, in 1921, a compulsory Act on Disablement Benefits was introduced, ensuring the disabled help without the loss of civil rights. The many individual acts that had been passed in the period from about 1890 to 1930 were combined and simplified through the great Social Reform Act of 1933. It was now generally established that financial aid to citizens as a result of some unforeseen occurrence should not limit civil rights; however, limitations were not completely abolished until the Public Assistance Act of 1961.

After the Second World War social legislation reflected a constant development in the welfare state; a number of acts were introduced covering special cases of need, including one for the deaf (1950), the blind (1956) and the mentally deficient (1959). In 1956, on the basis of an agreement with the two sides in the labour market, a sick pay scheme was established. In 1958 arrangements for home help were established, replacing the previous arrangement for mother's helps. A new Act on National Pensions and Disablement Pensions (1956) introduced the principle that everyone had the right to a pension irrespective of capital and income, and independently of former employment and income. Everyone over 69 was thus given entitlement to a minimum national pension.

In 1964 the Supplementary Pension Fund was introduced, a compulsory arrangement for employees, in which the pension depends on the contributions paid.

In 1973 a compulsory health insurance programme was introduced, funded from general taxation, and replacing the sickness benefit funds, and at the same time a reform of daily cash benefits was introduced, ensuring everyone against loss of income resulting from illness.

In 1976 the Social Assistance Act came into force. This introduced a single, unified structure, implying that the social assistance office in the local authority area must deal with the problems, irrespective of the reasons for social need. With this act, a principle of discretion was introduced, i.e. that support should be given from an overall evaluation of the client's situation. Since then a large number of changes have been made to the Social Assistance Act. Of central importance is that in

In 1987 the principle of discretion was changed to a principle of entitlement, which meant fixed rates for most forms of help. With effect from 1.7.1998, the Danish parliament passed a new Social Welfare legislation covering legal safeguards, social service, and active social policy.

### **1.3.2 UNEMPLOYMENT BENEFITS AND LABOUR MARKET POLICY<sup>4</sup>**

With the industrialisation process, the trade unions took over the guilds' tradition for mutual support to their members in the form of sickness insurance, unemployment insurance and employment service. Gradually the public sector stepped in and supported those schemes. An Act on Insurance against Accident came into force in 1898.

In 1907 a law was passed that provided public support for the unemployment insurance funds established by the state unions and thus established the Danish version of the "Ghent system" that has survived to today. In contrast to the public social security, the public support to the unemployment benefit funds was given without implying the loss of civil rights for anyone receiving help.

An anticipatory pension scheme ("Voluntary Early Retirement Scheme") was introduced in 1979, making it possible for 60-66-year-old members of an unemployment benefit scheme to withdraw from the labour market before reaching pensionable age. This benefit, like subsequent arrangements for leave and activation was established largely with a view to reducing unemployment.

Around WWII, labour market policy was gradually established as a separate policy area, distinct from social policy. Focus was no longer just on economic support for the unemployed, but also on labour mobility and wage formation. In 1969 the public employment service was established as a separate branch closely related to economic policy and embedded in a centralised system with strong corporatist elements. With the economic crisis of the 1970s and 1980s some convergence between the two systems was seen, mainly due to a more active profile for social policy. With the present reform of local and regional government that is described in more detail below, one may say that this convergence will take one step further. However, the distinction between those unemployed that are members of the unemployment insurance funds and the "un-insured" unemployed prevails, as a sign on the strong path dependency of this part of Danish society dating back more than a hundred years.

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<sup>4</sup> This section is built on Damgaard, 2003, chapter 3.

## **1.4 POTENTIAL THREATS TO THE DANISH MODEL**

This section outlines some of the major challenges facing the Danish flexicurity model in the next few years.<sup>5</sup> The structure of the section mirrors the three corners of the flexicurity triangle.

### **1.4.1 GLOBALISATION AND PERCEIVED JOB INSECURITY**

Globalisation and outsourcing of jobs to particularly South East Asia are often pointed out as the most important challenges to employment and welfare policy facing the Danish labour market, both at present and in the future. This has an effect on the employees' sense of job security and thus on their mobility willingness. It is a condition for the employees' willingness to change jobs or job functions that they feel secure, either at their present workplace or of their place on the labour market in general. All the media hype about globalisation and outsourcing has probably had a negative psychological effect on the mobility of the labour force. As already stated, the Danish labour market legislation and the collective agreements offer workers little job protection. It is this sense of job security and employment security that may be challenged by the threat of outsourcing jobs. It is also conceivable that e.g. employers have a strategic interest in inflating the ideas of the scale and nature of globalisation, as this rhetoric can help soften the trade unions and employees, and make them more accommodating of atypical forms of employment or lower wage demands. Skaksen (2004) maintains that the possibility of outsourcing in itself can have a disciplining effect in connection with collective bargaining, because wage restraint becomes an alternative to outsourcing of production.

### **1.4.2 TO WHAT EXTENT DOES GLOBALISATION AFFECT JOBS?**

The question still remains, however, if there is empirical support for the expectations of massive outsourcing of jobs, and to what extent globalisation will in reality affect the flexibility of the labour market.

The Danish National Institute of Social Research finds, on the basis of a study of sectors of industry particularly exposed to competition in the period 1997-2000, that competition from low-wage countries seems to have had few serious negative consequences for Danish workers (Geerdsen *et al.*, 2004). The Board of Economic Advisers (DØR) estimates, after reviewing a number of Danish studies on outsourcing of jobs, that around 5,000 jobs disappear every year from Denmark as a direct consequence of outsourcing (DØR, 2004: 132). As approx 260,000 jobs disappear or are

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<sup>5</sup> For a more detailed exposition, see Bredgaard, Larsen & Madsen, 2006.

created every year, outsourcing seems to account for a rather modest share of the dynamics of the labour market. The research-based knowledge available – sparse as it still is – on the scope and nature of outsourcing and off-shoring of jobs thus calls for a more sober-minded assessment of the problem.

Nevertheless, a number of factors seem to indicate that the particular Danish combination of high numerical flexibility, high social security and employment security means that both enterprises and workers are well armed to take up the challenge and meet the needs for change and adaptability constantly demanded by new technology and intensified national and global competition. The real challenge in connection with outsourcing of jobs may be to safeguard workers' rights, consumer safety, environmental standards etc. in the receiving country.

### **1.4.3 MOBILITY AND SOCIAL EXCLUSION**

The large number of job changes on the labour market means that the workforce is continually tested for their productivity and work potential. This constant selection process leads to some groups of employees being gradually excluded from the labour market if they fail to live up to the expectations of the employers. A large group of workers are thus more or less permanently balancing on the edge of the labour market or outside it. From 1960 to the mid-1990s, the number of people on transfer income grew from around 200,000 to 900,000 full-time persons, equivalent to a quarter of the adult population. The price for a highly efficient and mobile labour market with an extensive safety net therefore seems to be that a large part of the potentially active population of working age is gradually excluded from the labour market and become welfare recipients. It must be said, though, that the number of people on transfer income fell to approx. 800,000 by the end of 2002. Since the early 1960s the employment rate has been stable at about 75%. The growth in the number of people on transfer income thus coincides with a marked decrease in the number of persons (especially married women) who are provided for by their family (Madsen, 2003).

In contrast to this, the mix of the group of people on transfer income has changed considerably. Immigrants from third-world countries make up a growing share of social assistance recipients; they have considerably lower employment and participation rates than ethnic Danes, and this constitutes a huge and so far unsolved integration and labour market problem (Tænketanken, 2006). The number of long-term social assistance recipients also remained more or less unchanged during the 1990s' 'job miracle'. The number of long-term sickness benefit cases also shows a marked increase in recent years, which may of course have any number of causes, including the ever-faster pace and productivity race in the labour market. As can be seen, there are still unsolved marginalisation and

social exclusion problem on the Danish labour market – although in a comparative perspective, they seem less severe than in other European countries (cf. Bredgaard, 2004a; 2004b). The low degree of job protection probably plays a double role in this connection for ‘weak’ groups on or outside the labour market. On the one hand, employers need not be fearful of hiring somebody from the so-called weak groups as it is relatively easy to fire them again. On the other hand, employers may be less inclined to focus on prevention and retention of employees in the workplace. Thus both exit and entry into the Danish labour market are easy, also for disadvantaged groups.

#### **I.4.4 THE CHALLENGES TO INCOME SECURITY**

The high rate of income compensation in case of unemployment (up to 90% for certain low-income groups) increases the risk of economic disincentives, especially for low-income groups. Even though such incentive problems seem plausible, both theoretically and intuitively, they are nevertheless difficult to prove empirically, at least on a larger scale (cf. Goul Andersen *et al.*, 2003). One reason could be that potential disincentive problems, in particular in connection with the labour market policy, have been sought remedied in the form of tighter availability and mobility demands, early and intensive activation and the ‘right and duty’ to activation – rather than reductions in the level of benefits.

#### **I.4.5 CHALLENGES TO THE ACTIVE LABOUR MARKET POLICY**

Since 2002 adjustments of the labour market policy have gradually moved the policy in the direction of more disciplining: the eligibility period for unemployment benefit has been further reduced, sanctions, availability and mobility rules tightened, and the skills upgrading elements reduced. At the same time there has been a gradual roll-back of the responsibilities of the regions and the social partners. When the labour market policy is re-calibrated towards more social disciplining (*i.e.* work first), it implies seeking to increase the motivational effect rather than the upgrading effect (*i.e.* human capital), which may be linked to some effect measurements of the activation measures, which have claimed, among other things, that education can in fact have a negative effect on the subsequent self-sufficiency rate of the individual, and that on the whole only private job placement can demonstrate any positive effects (Geerdsen, 2003). Together with new evaluations, this provides the basis for increasing focus on the importance of the effects of motivation and threats in the labour market policies (Rosholm & Svarer, 2004). Typically, the effect evaluations made so far have focused on short-term effects of specific measures, whereas there is much less knowledge about the longer-term impact of combined measures, *e.g.* initiatives involving education and training followed

by work experience or subsidised job-training (cf. Hansen *et al.*, 2005 for an analysis of the long-term effects of educational measures).

Giving lower priority to the training and education aspects of the active labour market policy may, however, have consequences for the flexibility on the labour market, especially in a situation where the individual's reasons for unemployment are more related to the *ability* (lack of qualifications or work experience etc) than to his or her *willingness* to work (financial incentives) (cf. Goul Andersen *et al.*, 2003). A growing mismatch between the labour market policy's 'medicine' and the patient's 'illness' can thus emerge, which will diminish the possibilities of (re)integrating the marginal groups of the labour market, to the detriment of both dynamics and flexibility on the labour market (Bredgaard, 2005).

The intention of adopting a one-tier system instead of a two-tier system presents a number of both potential opportunities and risks in relation to labour market flexibility. There are, for instance, obvious advantages from coordinating the activities of the public employment service and those of the municipalities, *i.e.* the state and municipal labour market policy. However, localising labour market policy entirely to the municipalities runs counter to one of the previously fundamental principles of labour market policy: that employment policy is to be managed on the basis of functional, and not geographical, considerations (cf. Jørgensen *et al.*, 1999). An important point of criticism from labour market organisations has indeed been that a one-tier, municipalised employment system might hamper labour mobility across local authority boundaries.

In spite of these breaches with traditional labour market policy, one thing remains unchanged – the role of the enterprises. Danish labour market policy is still very supply-side oriented, that is, oriented towards activating the unemployed. It has no tradition for involving and no instruments established to activate enterprises, apart from a policy of corporate social responsibility, which is at the moment considerably less ambitious than it used to be. In order to get more people employed and to increase the supply of labour it is, nevertheless, an essential precondition that enterprises on the one hand choose to retain employees in danger of social exclusion (e.g. older or disabled workers), and on the other hand help integrate people who have already been excluded (cf. Bredgaard, 2005).

As already hinted throughout this summarised review of the challenges to the flexicurity triangle, the Danish flexicurity model is not an unchangeable construction. Changes are happening around all corners of the triangle important to the flexibility, dynamics and functioning of the labour market. It is important to bear in mind that there is a dynamic interaction between the flexible labour market,

income security and the active labour market policy, and that changes in any one of these elements will therefore have consequences for the others. Each of the elements are being challenged at the moment by trends such as globalisation, changes in the security systems and changes to the labour market policy. The question then is whether any of these changes are of a scope and a nature which justifies talking about fundamental systemic changes, which will change the Danish flexicurity model for good, or whether what we are seeing are just minor alterations. It is probably still too early to tell.

What is important to point out in this context is the fact that the precondition for the resilience of the model is continuous support from the social partners, and confidence in the ability of the model to secure a balancing of social and political compromises. The particular Danish variety of corporatism, in which the labour market parties are involved in the drafting of legislation and decision-making processes, and share responsibility for implementation, is no doubt an important condition for the development and robustness of the flexicurity model. It is on these points that the model will be facing challenges in the coming years, as a consequence of the ongoing local authority reforms, which will, among other things, have an effect on the social partners' scope for influencing the policy and in the longer term also the design of the income provision system for the unemployed (e.g. as a result of a beginning blurring of boundaries between local authority economy and the unemployment benefit system).



## **2 EMPLOYMENT PROTECTION**

### **2.1 MAIN ELEMENTS OF THE SYSTEM**

As described above, Denmark is normally ranked as a country with a rather low level of employment protection (e.g. OECD, 2004: chapter 2). However, in reality the situation is somewhat more complex and implies different levels of protection for different groups. First of all, and as an important general observation, one should point to the fact that employment protection in Denmark is, to a large degree, seen as an issue to be handled by the social partners as part of the general negotiations over work and pay conditions. Therefore, one will find only limited legislation in this field.

One important exception is, however, the “Law on salaried workers”, which regulates the employment conditions for large groups of white-collar workers. In the law itself, a salaried worker is defined as a person, who conducts office work, clinical work and similar functions or supervises the work of others. However, in many collective agreements it is stipulated that those workers covered by the agreement will have right as defined by the law, even if they are not covered by the definition in the law itself. It is the assessment that the majority of public employees and about half of the employees in the private sector are covered by agreements or regulations that follows the “Law on salaried workers”.

The law stipulates among other things, a set of rules for dismissals, whose main content is a definition of the employer’s notice period in relation to the duration of employment. An increasing number of non-salaried workers in the private sector have, as parts of the negotiations between the social partners, been classified as “quasi-salaried worker” and therefore will experience a level of employment protection similar to those just described. Employers offending the protection of salaried or quasi-salaried will have to pay compensation to the former employee. However, the employer cannot be forced to reinstall the employee into employment. Apart from these groups, one may in the collective agreements for different groups and sectors find varying rules concerning employment protection. The lowest protection level is found in the construction sector, where one can find dismissal periods down to one or a few days. This is discussed in more detail in section 2.2.

Concerning part-time workers, there are no specific regulations, with part-time workers being covered by the same regulations as full-time workers – a situation which is a general feature of the Danish labour market. Due to the rather low level of employment protection on the Danish labour market, the share of persons having a time-limited contract is rather low. The use of such contracts is now regulated by rules that implement the EU-regulations in this area.

Finally, one should mention that legislation has been introduced to ban the discrimination of pregnant women, when it comes to dismissals. Thus employers who dismiss pregnant women will have to prove that the dismissal had nothing to do with the pregnancy and face a fine and payment of compensation to the former employee, if this cannot be proved.

Cases brought against employers for offending the regulations with respect to employment protection are handled by the separate legislative system that is established for the labour market.

## 2.2 EMPLOYMENT PROTECTION IN PRACTICE

Table 2.1 gives some examples of the notice periods for different groups of employees. As mentioned above, it is the assessment that the majority of public employees and about half of the employees in the private sector are covered by agreements or regulations that are equivalent to those of salaried workers in Table 2.1.

Table 2.1: Notice period by duration of employment and occupational group

Duration of employment	1 year	5 years	10 years
Construction worker	3 days	5 days	5 days
Industrial worker	21 days	2 month	3 months
Salaried worker and public employee	3 months	4 months	6 months

Source: Westerlund (2006), Table 5

Similarly, Table 2.2 shows the severance pay, which is paid to salaried workers with a high tenure, but rarely to blue-collar workers.

Table 2.2: Severance pay by duration of employment and occupational group

	12 years	15 years	18 years
Salaried workers	1 month's wage	2 month's wage	3 month's wage
Blue collar workers	Found in some collective agreements		

Source: Westerlund (2006), Table 6

Unfortunately, there it is difficult to get a statistical overview of the functioning of the system of employment protection as a whole, because most of the conflicts are solved through arbitration at the firm level involving the local trade union representative and the local employer's organisation. Only a few of the dismissal cases therefore reach the Court of Labour (see [www.arbejdsretten.dk](http://www.arbejdsretten.dk)).

A further observation to be made is that the low level of employment protection is correlated with a relatively small share of employees having an employment contract of limited duration. According

to the latest labour force survey for 2005 only 9.9 percent of the employees have such a contract. The share is highest – at about 20 percent - for young persons aged 15-29 years among which one will find many students having some form of temporary job. For the EU-15 the average share of persons with fixed term contracts is around 13 percent. There is a minor gender difference in the sense that 11.3 percent of the women have a temporary contract, while the share for men is 8.7 percent.

Concerning part-time work one should note that this is covered by the same agreements and regulations concerning dismissals as full time work.

Furthermore, it should be mentioned that the anti-discrimination laws prohibits employers from dismissing employees due to pregnancy and also forbid discrimination due to gender, race, age etc.

Turning to possible explanations for the low level of employment protection on the Danish labour market a few candidates are mentioned in the literature.

Firstly one may point to the fact that although 62 percent of the employees are found in firms with more than 100 employees, the majority of Danish firms (defined as workplaces) are small. Of the 283,000 firms existing in 2004, 78 percent had less than 10 employees, while 15 percent has between 10 and 49 employees. Only 3 percent had more than 50 employees.<sup>6</sup> In such an environment it is less functional to impose large restrictions on the employer's rights to dismiss staff.

Secondly, almost all Danish Governments in the 20<sup>th</sup> century were based on coalitions involving centre parties – and on in a two-year period in the 1960s the Government was based on a socialist majority. Thus in contrast to for instance Sweden, it was politically difficult to impose strict EPL-legislation based on a traditional interpretation of worker's interests. Also in this area, Danish policy-making proved its tradition for class-compromise and consensus (Jørgensen, 2002).

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<sup>6</sup> Calculations based on the databanks of Statistics Denmark.



### **3 UNEMPLOYMENT INSURANCE**

As stated in Section 1, the main features of the Danish system of unemployment insurance date back to the early years of the 20th century. It was given its present form in a large reform in 1969. The economic support to unemployed will come from either the unemployment insurance funds or from the social assistance system administered by the municipalities.

#### **3.1 THE PRESENT SYSTEM OF UNEMPLOYMENT INSURANCE**

In the following sections the main features of the present system are explained.

##### **3.1.1 THE UNEMPLOYMENT INSURANCE FUNDS**

Unemployment insurance is regulated by a separate law and accompanying regulations. The chapters of the law determine in great detail:

- The criteria for becoming a recognised unemployment insurance fund (including a minimum of 10,000 members);
- The criteria for becoming a members of a recognised fund;
- The rules for calculation and payment of unemployment benefits;
- The rules for the special Voluntary Early Retirement Scheme;
- The calculation of membership contributions;
- The calculation of the state contribution to the funds;
- The rules for employer's obligation to pay the unemployment benefit during the first two days of unemployment of a previously employee;
- The sanctions imposed on members to receive benefits without being eligible to these;
- How the funds shall be supervised by the Labour Directorate; and
- The rights of members with respect to complaints over decisions made by the funds and the Labour Directorate.

According to the law, sanctions will be imposed by the funds on individual members that receive unemployment benefits without being eligible (for instance if they are not available for work or do not actively look for work). The standard sanction is withdrawal of benefits for a shorter period of time (e.g. three weeks).

### 3.1.2 MEMBERSHIP CONDITIONS

Membership of an unemployment insurance fund is voluntary. Members have to fulfil the following criteria:

- A member must stay and reside in Denmark. However, departures are made from this rule if the person resides in another EEA country;
- They must be between 18 and 63 years of age, when they join the unemployment insurance fund. The age limit of 63 years for joining the funds is due to the fact that one must have been a member for one year before being eligible to benefits and benefits are only paid to persons aged less than 65 years, which is the pension age for public old age pension (*cf.* below);
- They must have employment as an employed person or as a self-employed person or assisting spouse in a company owned by a self-employed; and
- A person can also be admitted as a member of an unemployment insurance fund if the person has completed a vocational training course of at least 18 months' duration when you apply for membership not later than 2 weeks after completion of the training course.

Both full-time and part-time employees can become members of an unemployment insurance fund. Part-time insurance is an option for persons working less than 30 hours per week. Both membership contribution and unemployment benefits are lower for this group. Thus benefits cannot be higher than two-thirds of the benefits for a full-time insured person.

### 3.1.3 MEMBERSHIP CONTRIBUTIONS

The membership contribution amounts to:

- A flat-rate compulsory contribution to the unemployment insurance, which is the same for all members and in 2006 amounts to 3,204 DKK pr year (430 Euro)<sup>7</sup>;
- A flat-rate contribution to finance the Labour Market Supplementary Pension Scheme (the so-called ATP-scheme);
- An administrative fee, which varies (considerably) between the individual unemployment insurance funds (*cf.* section 3.3.3 below); and
- A voluntary early retirement contribution for the Voluntary Early Retirement Scheme. The early retirement contribution in 2006 amounts to DKK 4,668 for full-time insured members. Early retirement contributions are payable only, if you want to be covered by the early retirement benefit scheme. The benefits paid under this scheme are related to the level of unemployment benefits and will not reflect the individual amounts contributed by the member, if the member

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<sup>7</sup> The current exchange rate is 7.44 DKK to 1 Euro (November 2006).

fulfils the eligibility criteria. These call for a certain minimum number years of having contributed to the scheme (at present 25 years). The member can retire from the age of 60 years.

All membership contributions are tax deductible, which implies that the net cost to the member is about two-thirds of the gross cost.

The amounts are adjusted at each turn of the year (according to the wage-index). An important observation is that the membership contribution is not based on actuarial considerations about risks of unemployment for individuals or group, but is uniform for all members, notwithstanding which fund they are members of.

### **3.1.4 LEVEL OF UNEMPLOYMENT BENEFITS**

To be entitled to unemployment benefits, the unemployed must in general fulfil the following conditions: (1) Have been a member of an unemployment insurance fund for at least one year; and (2) For persons insured on a full-time basis, the employment requirement means that they must have had employment to such an extent that it altogether corresponds to employment during the full, normal working hours of the trade or profession for a minimum of 52 weeks within the past 3 years. If the full, normal working hours are 37 hours a week, the employment requirement for full-time insured members will amount to a total of 1,924 hours of work within the past 3 years.

Furthermore the unemployed must look actively for work and is subject to the rules and regulations of active labour market policy (*cf.* below). In principle an unemployed person, who has been unemployed for more than 3 months, must accept any job offered by the Public Employment Service (PES) that the person can perform. By example an unemployed academic must willing to work as a postman. However, in practice the PES is not very strict implementing this rule, because of the expected lack of motivation of the unemployed if actually employed in the job.

Taking part in labour market training will not make the unemployed eligible for an extension of the benefit period. Not complying with this will lead to suspension of benefits and ultimately to expulsion from the insurance system. Suspension can be for one week and up to 26 weeks. For 2004, the statistics of the Directorate of Labour shows that approx. 3,500 persons had their benefits suspended for more than 3 weeks (Arbejdsdirektoratet, 2005).

The benefit rate is individual and depends, among other things, on the size of the previous earned income. Unemployment benefits can, at a maximum, amount to 90 percent of previous earnings.

The maximum benefit rate in 2006 is 667 DKK (90 Euro) per day for full-time insured members. Unemployment benefits are paid out for 5 days a week. The maximum yearly benefit is therefore 173,420 DKK (23,278 Euro).

Once being eligible for unemployment benefits, an unemployed person may collect them for a total period of 4 years, if s/he follows the directions concerning active job seeking and participation in active labour market programmes (cf. below). After the end of the four-year period, the unemployed loses the right to unemployment benefits and will have to apply for cash benefits as an “un-insured” unemployed, cf. below. The right to benefits is also automatically lost at the age of 65 years, where the person will qualify for old-age pension.

### **3.1.5 THE NON-INSURED UNEMPLOYED**

Apart from those having exhausted their right to unemployment benefits, the group of “non-insured” unemployed consist of those unemployed, which do not fulfil the criteria for becoming eligible to unemployment benefits in the first place (cf. the list of criteria presented above). This group of unemployed must apply for cash-benefits administered by local government (the municipalities). Cash benefits are means-tested and the amount depends on the family-situation of the unemployed. By example a person aged 25 and more and having children will receive 139,500 DKK per year (18,725 Euro), while a young person aged 24 and less will receive 67,656 DKK per year (9,081 Euro). The duration of cash-benefits is not limited, but again the person will have to accept the offers from the municipality to participate in active programmes. If not, cash-benefits may be reduced or abolished all together.

These benefits are thus considered as parts of social policy and regulated by a separate law under the supervision of the Ministry of Employment. Financing is shared between national Government and the municipalities.

Complaints over cash benefits (eligibility and calculations of amounts) are handled by a separate public body under the Ministry of Social Affairs.

## **3.2 DISTRIBUTION OF RESPONSIBILITIES**

The Labour Directorate, which is a separate body under the Ministry of Employment, is responsible for the implementation of the law on unemployment insurance and for supervising the activities of the unemployment insurance funds. The Directorate of Labour also handles complaints from

members over the administrative decisions made by an unemployment insurance fund. The tight supervision is of course due to the fact that the unemployment insurance funds are responsible for administering large amounts of public money.

Each unemployment insurance fund is formally an independent association, where the members elect a board, which again is responsible for the day-to-day operations of the fund. In practical term, since most of the funds are closely connected to one or more trade unions, the election of the boards is heavily influenced by the trade unions and is rarely subject to much debate among the members. A further reason for this is of course that the tight public regulation of the system (including the benefit levels) leaves little room for discussions about the activities of the individual fund.

At the national level the unemployment insurance funds have formed a national organisation, which presents the interests of the funds vis-à-vis the Labour Directorate and the political system.

The Directorate of Labour is responsible for the recognition of new funds and for supervising the legality of the existing funds. To become registered as an unemployment insurance fund and to remain within the system, the fund has to have at least 10,000 members. If a fund does not fulfil the criteria or live up the regulations, the Labour Directorate can withdraw the public funding totally or partly.

One recent trend in the development of the funds has been related to a series of benchmarking exercises conducted by the Directorate of Labour. The studies revealed considerable differences in the cost levels and efficiency of the funds and therefore has put more focus on the size of the part of the membership contributions, which is related to the administrative costs of the funds. This has lead to an increased competition among the funds. The competition has furthermore been stimulated by recent changes in the legislation, which makes it easier for individuals to choose between different funds (the principle of free choice among unemployment insurance funds).

As part of the attempts to give a more active and job-oriented profile to social policy, the responsibility of the non-insured unemployed at the national level was moved from the Ministry of Social Affairs to the Ministry of Employment in 2001. Also, as part of the so-called structural reform of the public sector in 2007, responsibility for active measures for both the insured and the non-insured unemployed will be integrated into “job centres” in the municipalities, but without integrating the responsibility for the financing and payment of benefits to the two groups.

Parallel to the cash benefits for the non-insured unemployed, the municipalities are also responsible for the other elements of social policy, including administration and payment of sickness benefits and other social benefits (e.g. disability benefits).

The Danish unemployment benefits system therefore still has the character of a two-tier system divided into the members and the non-members of the unemployment insurance funds. Although the overall organisation of Danish labour market policy is right now being reformed as part of the general structural reform of the public sector (cf. below), this two-tier system will remain intact in the foreseeable future. Apart from this two-tier character, the system is nationwide and uniform in the sense that it does not differ across sectors or occupational groups.

Finally, one should mention that as a reflection of the anticipated need of some wage earners to supplement the normal benefits of the unemployment insurance funds, a number of funds and trade unions have during the last five years introduced supplementary unemployment insurance schemes, in cooperation with private insurance companies. The schemes are marketed as part of the attempts of the unions to attract members by offering a new package of services (also including for instance individual career advice, further education, discounts on vacation etc.).

Since the premiums are calculated on a purely actuarial basis, the premiums paid are rather high compared to the level and duration of the supplementary benefits and it is also subject to frequent changes depending on the development in the risk of unemployment. By example at present, an office worker wanting to have a supplementary benefit during a maximum of 12 months of unemployment amounting to a sum equal to the normal amount of benefit, will have to pay a premium of about the same size as the normal membership contribution to the unemployment insurance fund (the latter having a maximum benefit period of four years).

The maximum coverage offered by the insurer may amount to twice the amount of normal benefits, but with a total maximum of normal benefits and supplementary benefits of about 80-90 percent of previous income. Since there are no laws regulating the supplementary insurance schemes, the coverage and prices are based solely on the insurer's assessments of actuarial risks and other costs of the schemes.

In 2004 it was estimated by the Danish Insurance Association that 1.7 million of the nearly 2.4 million members of unemployment insurance funds had the opportunity to take such a supplementary insurance, because their unemployment insurance fund had an agreement with a private insurance company (Forsikring & Pension, 2004: p.14). There are no comprehensive statistics

showing the total number of persons actually having taken such an insurance, but it is estimated that the number is as low as 50,000 persons or about 3 percent of the potential number. However, the Danish Insurance Association expects the share to rise rapidly in the coming years due to the low level of coverage offered by the normal unemployment insurance funds, when it comes to wage earners with medium or high incomes.

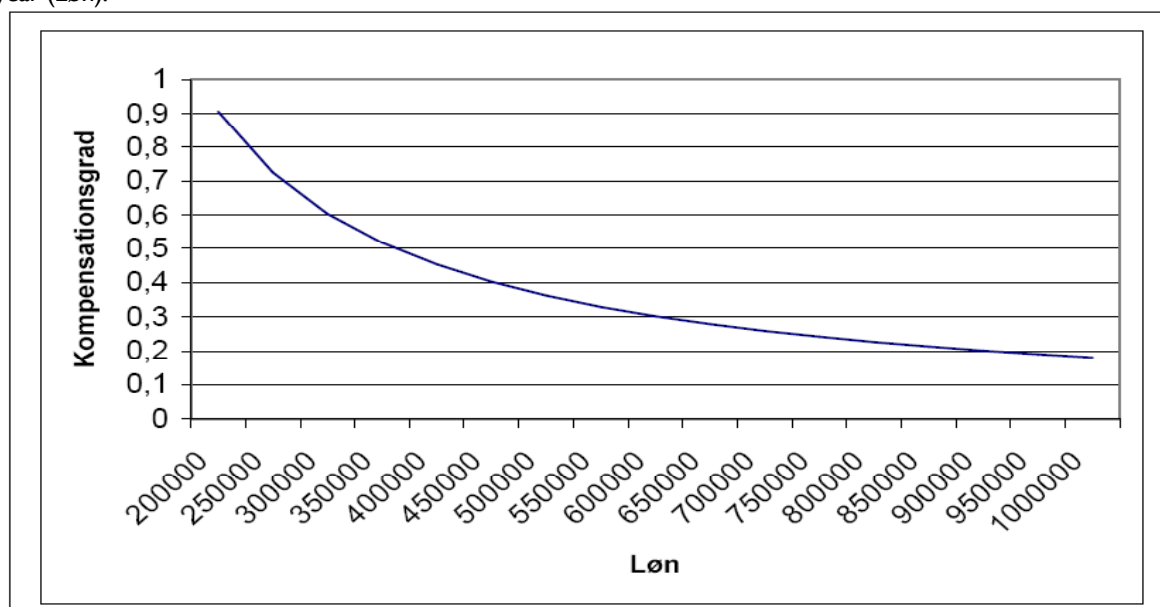
### **3.3 FIRST ORDER EFFECTS**

#### **3.3.1 REPLACEMENT RATES**

As presented in the description of the calculation of unemployment benefits, they amount to 90 percent of previous earnings (normally calculated over a three month's period before becoming unemployed). There is a maximum amount, at present equal to approx. 14,500 DKK per month. As shown in Figure 3.1, this implies that the gross compensation rates declines rapidly with previous income, when the income reaches a limit of about 200,000 DKK per year. To give an impression of the groups actually experiencing the different levels of gross compensation one can mention that a wage earner in the private sector at the lowest income level would get about 175,000 DKK (excl. pension) per year in 2005, while an average salesperson would get 235,000 DKK per year. A highly skilled white-collar worker would earn 457,000 DKK per year (Dansk Arbejdsgiverforening, 2006: Table 5.28).

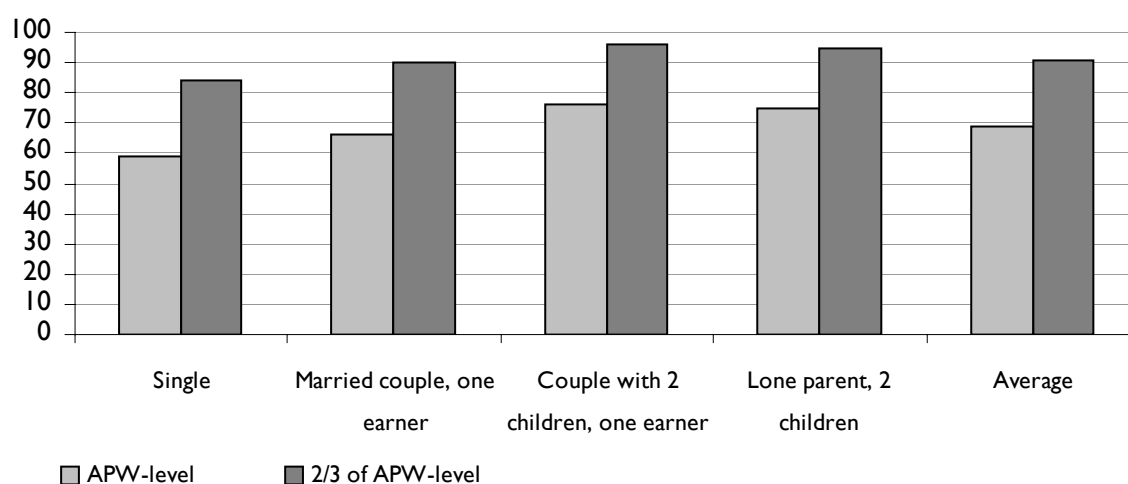
The OECD calculates the net compensation rates for different family types and income levels (Figure 3.2). As it is evident from this figure – and as a consequence of the limit on the unemployment insurance benefit - wage-earners earning 2/3 of the average production worker (APW) experiences a significantly higher rate of compensation than the average worker. Also, the family situation plays a (limited) role, which is not due to the unemployment insurance system, but related to other benefits (like housing benefits), which are included in the OECD-calculations.

Figure 3.1: The gross rate of compensation (Kompensationsgrad) for earned incomes above 200,000 DKK per year (Løn).



Source: LO (2006), Figure 3.1

Figure 3.2: Net replacement rates for two income levels and four family types (the first month of benefit receipt), 2002.

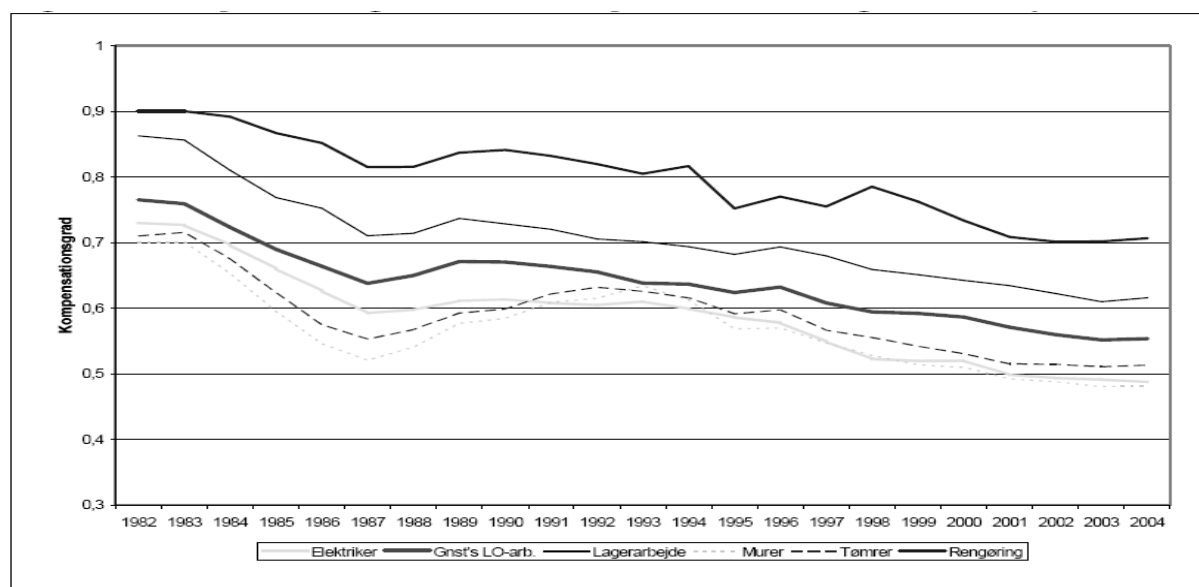


Source: OECD (2004): *Benefits and Wages 2004*, Tables 3.1b and 3.3b

As illustrated in Figure 3.3, over the last decades there has been a tendency for the compensation rates to decline, which has caused some debate. The main reason for the decline is a special and rather complicated system for indexing the development of unemployment benefits (and other transfer incomes) to the increase in average wages. The main element of the indexation involves regulating unemployment benefits with the percentage increase in yearly wages (excluding pensions and paid absence) two years before with a deduction of 0.3 percentage points. This deduction is used to finance targeted measures for special groups among the unemployed and other “weak

groups". Furthermore the introduction of collective pension schemes among blue-collar workers has led to a decline in the compensation rates, because contributions to such schemes are not included in the calculation of unemployment benefits. As a result, the compensations rates (including pension contributions) have gradually declined since 1982, as shown in Figure 3.3.

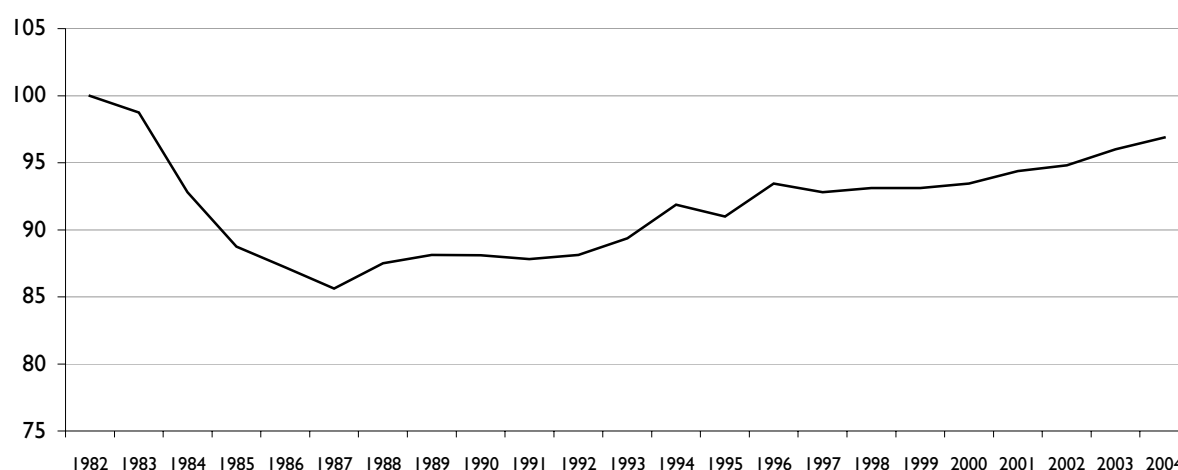
Figure 3.3: Compensation rates for different groups of blue-collar workers 1982-2004.



Note: "Elektriker" = electrician, "Gnst. LO-arb" = average LO-worker, "Lagerarbejde" = warehouse worker, "Murer" = bricklayer, "Tømrer" = carpenter, "Rengøring" = cleaning

Source: LO (2006), Figure 3.3.

Figure 3.4: Real purchasing power of unemployment benefits (1982=100), 1982-2004.



Source: LO (1996), Figure 2.1

Finally, as shown in Figure 3.4, the purchasing power of unemployment benefits has been almost unchanged over the period 1982-2004, but with large fluctuations mainly due to different shifts in

the indexation of the benefits, including the years 1983, 1984 and 1985, where the benefits were “frozen” (meaning not regulated at all).

### 3.3.2 COSTS AND FINANCING

As previously described, the major part of unemployment insurance is financed by the state. The total expenditure for unemployment benefits was 20,405 million DKK in 2005. The other major payments from the unemployment insurance funds are for the voluntary early retirement pay, which amounted to 24,147 million DKK in the same year. The costs are covered from three sources: the mandatory contributions to unemployment insurance from the members, the voluntary membership contributions to the Voluntary Early Retirement Pay (VERP) and the states. Table 3.1 gives an overview.

Table 3.1: Revenue and costs of the Danish unemployment insurance system, 2005

Item	Amount (million DKK)
Unemployment benefits	20,405
Voluntary Early Retirement Pay	24,656
Total expenditures	45,061
Covered by:	
Membership contribution to UI (mandatory)	7,068
Contribution to VERP (voluntary)	5,712
State contribution	32,281

Source: Data provided to the author by the Directorate of Labour

To the costs in Table 3.1 can be added the administrative costs of the Labour Market Directorate (approx. 180 million DKK) and the administrative costs of the individual unemployment insurance funds (covered by the members). In 2004 the total administrative costs of the unemployment insurance funds amounted to 3,300 million DKK (Arbejdsdirektoratet, 2005, p. 15). One may also add the costs of the active labour market programmes for the insured unemployed members of the funds, which adds up to 7,518 million DKK.

In 2005 the total administrative costs of the unemployment insurance funds were 3,200 million DKK, which was covered by the membership contributions. Thus, of the total memberships contributions about 20 percent covers the administrative costs of the funds, while 44 percent is the mandatory membership contribution to the unemployment benefits and the remainder 36 percent are contributions to the voluntary early retirement scheme.

Since the state covers all variations in the expenditures of benefits through the state budget, no special funds are accumulated. Membership contributions are not regulated according to the general

level of unemployment or the unemployment risks of the individual member or groups of members. The only factor that makes the membership contributions differ between the funds is the variations in the administrative costs of each fund, cf. below.

Since the funds are formally private organisations, they could in principle suffer bankruptcy, if for some reason they were not able to cover their administrative costs due to lack of membership. However, no such examples have been seen. The normal procedure for an unemployment insurance fund in financial trouble is to merge with another fund. This will also be the case, if a fund fails to fulfil the criteria for a minimum number of members of 10,000 persons.

### **3.3.3 THE ADMINISTRATIVE EFFICIENCY OF THE UNEMPLOYMENT INSURANCE FUNDS**

Since 2001, the Directorate of Labour has conducted regular studies of the administrative efficiency of the unemployment insurance funds. On average the funds spend 6 DKK on administrative purposes for every 100 DKK that they pay to their members. The total number of employees in 2005 was about 5,000, a slight reduction by 5.5 percent from the level in 2000 (Arbejdsdirektoratet, 2005)

It is however a striking observation that there are large differences between the administrative costs per member between the cheapest and the most expensive fund (in the range from 624 DKK to 2,748 DKK per year). The level of unemployment of the members and the number of unemployment spells per member will of course play a role in explaining these differences. So will the number of local offices and service level. However, measured per transaction there are still huge disparities, which must be explained by differences in the level of productivity. Thus the unit cost of a transaction differs with a factor of three between the least efficient and the most efficient fund. According to the Directorate of Labour this points to a considerable potential for lowering the administrative costs of the insurance funds, which is of course one of the main aims of this benchmarking exercise.



## 4 ACTIVE LABOUR MARKET POLICIES

### 4.1 THE ORGANISATION OF ACTIVE LABOUR MARKET POLICY

#### 4.1.1 AT PRESENT: A TWO-TIER SYSTEM

An important feature of the present system of labour market policy is its two-tier nature, which follows the dividing lines in the unemployment insurance system. At the individual level, the dividing line is therefore between those unemployed, who are members of an unemployment insurance fund, and those who are not and therefore eligible for means-tested social welfare. The former group is managed by the regional labour market authorities, and the latter are the responsibility of the municipalities. Since the two groups often have the same kind of difficulties, the set of instruments used, the timing of programmes (and also the level of benefits) are to a large degree parallel between the two systems.

Measured in numbers, the municipalities take responsibility for almost half of the total number of unemployed persons in active measures and thus play a key role in the implementation of active labour market policies. This is also the main reason for the present efforts to integrate the state system for the insured unemployed with the activities of local government, cf. below.

At level of the municipalities and in order to coordinate the activities of the actors involved in social and labour market policy at the local level, *social coordination committees* [*sociale koordinationsudvalg*] are established by law. A social coordination committee is a committee which is to advise the municipal authorities about preventive social measures. The committee is to contribute to developing the cooperation between the municipal authorities and various partners in the public and the private sector (including the social partners) in relation to their labour market programmes. The aim of the work of the coordination committees is to ensure that as many people as possible are given a chance of preserving their labour market attachment or becoming integrated on the labour market. The committees are thus to contribute to promoting employment opportunities for persons who are at risk of losing their job or persons with difficulties in obtaining employment on ordinary terms.

A coordination committee is composed of representatives of the municipal authorities, the social partners, medical advisers, handicap organisations and the public employment service. Each social coordination committee will cover a single or only a few municipalities. Compared to the Regional Labour Market Councils, the social coordination committees have only limited resources for

financing their own project and therefore act mainly as instruments for exchange of information and coordination of various activities.

#### **4.1.2 THE STRUCTURAL REFORM AND THE REORGANISATION OF LABOUR MARKET POLICY**

In 2006 and 2007 the so-called “Structural Reform” will imply major changes of the Danish public sector. The number of municipalities will be reduced from the present level of 271 to around 98. The 14 counties will be replaced by 4 regions having the health care system as their major assignment. A separate set of regions will be established with respect to labour market policy, cf. below.

The present 14 labour market regions (each headed by a director and a tripartite council) will be replaced by 5 labour market regions – each still with a tripartite council. The latter will however have lesser responsibilities than before. The reform thus implies two important changes compared to the present set-up:

- The role of local government in implementation of labour market policy will increase; and
- The influence of the social partners is reduced (probably as the outcome of some resistance from the present Conservative-Liberal Government and the Ministry of Employment towards the more powerful role of the social partners under the previous system).

At the level of the municipalities, the reform implies the creation of new job centres – one for each municipality. The job centres will be responsible for both the insured and the uninsured unemployed and will thus combine the tasks, which are now solved by the social assistance branch of the municipalities and the public employment service. However, apart from 10 pilot job centres, the formal legal responsibility for the unemployed will still be divided between a state-branch and a municipality-branch of each job centre. The model is thus a hybrid between a one-tier and a two-tier system.<sup>8</sup>

A major advantage of the new institutional set-up is that it – albeit still formally a two-tier system – allows for a much closer coordination and cooperation between the civil servants from the (present) public employment service and the social assistance branch of the municipalities. Thus the competences of the former PES-staff (focused on the demand for labour) and the social assistance

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<sup>8</sup> For an official overview of the reform, see [http://www.bm.dk/fremtidig\\_beskaeftigelsesindsats/default.asp](http://www.bm.dk/fremtidig_beskaeftigelsesindsats/default.asp). A more recent detailed description of the tasks of the new job centres can be found on the homepage of Local Government Denmark: <http://www.kl.dk/336499/> in the publication: “Temaguide om beskæftigelsesområdet – opgaveændring og sammenlægning”, October 13, 2005. For a recent overview of the new organisation of employment policy, reference can be made to Arbejdsdirektoratet (2006): *Styring, planlægning og opfølgning i det nye beskæftigelsessystem*, København ([www.adir.dk](http://www.adir.dk))

officers (focused more on the social problems of the individual clients) will come together in the new job centres.

The reform should also allow for a more transparent administrative system and reduce the need for sending both unemployed and firms from one public office to another. In principle the job centres will be able to handle all labour market related matters.

A third advantage is that the new system provides a simpler line-of-command from the national to the local level. An important reflection hereof is that the legal basis for active labour market policy will be included in a single act compared to the present situation, where you have separate pieces of legislation for the state branch (the PES) and the municipalities.

While the reform has, not surprisingly, been strongly supported by the representatives of local government, it has met strong criticism from both the social partners and a number of independent observers. The major points raised in this connection are the following.

At the local level the hybrid character of the new job centres with two categories of staff (the state employed and those employed by local government) and a corresponding divided management may create problems in the implementation and functioning of the reform. In the original proposal for the reform, a total transfer of the PES-staff to the municipalities was foreseen, but during the political process the present result came out as a compromise between different political parties. A review of the reform will take place in 2010 and will include the experiences from the 10 pilot centres, where a full integration takes place.

Given the limited size of the labour market, which is covered by each job centre, there is a risk that labour market policy will become too local in its focus and not take the larger regional (im)balances into account. An important task of the new regional organisation is of course to reduce this risk, but the problem is whether the new authorities at the regional level are powerful enough to overrule local interests. For the largest of the new municipalities and for lower skilled groups, the disadvantages from a narrow local focus are probably limited. However, about half of the new municipalities will have less than 50,000 inhabitants and for them – and for higher educated groups like academics - the geographical area covered by each of the new the job centres may be too small.

The smallness of some job centres also entails the risk of lack of specialised competences, when it comes to specific groups on the labour market. Here again academics can be mentioned as an example.

In the reform, this risk is expected to be controlled through further extending the use of private service providers (in Danish terminology often referred to as “other actors”). While this may solve the problem due to lack of competences in the smaller job centre, it also raises new demands on the specific skills needed to handle such private service providers, when it comes to defining contractual terms and the economic and legal incentives to be applied.

A further set of issues linked to the implementation of the reform at the local level is related to the relation between the economic resources for labour market policy and the economy of the local government as a whole. Given the risk of having the claims for resources for active labour market policy compete with other local spending (like care for the elderly or childcare), the reform implies water-tight sheds between spending for labour market purposes and other spending. This however raises the question of how to create economic incentives for the municipalities to an efficient use of resources allocated to labour market policy, if the economic gains from a more active effort are not available for other purposes. At present the whole set-up concerning the economic aspects of the reform are not fully transparent.

Finally, at a more practical level, the integration of the different administrative systems (including IT-systems) used by the municipalities and the PES poses a whole set of administrative and technical challenges, which will have to be overcome during the next year.

At the regional level, the weakening of the competences regional labour market boards entails the risk of dismantling the tradition for having an overarching plan for creating a better match between regional demand for and supply of labour.

Concerning the implementation of a *national strategy* for labour market and employment policy, the reform on the one hand increases, as mentioned above, the potential for implementing such a strategy. But on the other hand, Denmark has a long tradition for self-determination at the level of municipalities, exemplified by having the municipalities collect their own taxes. There is therefore a risk that the new and larger municipalities will pay more attention to local political interests than to strategies formulated at the national level. On the other hand, if the response by the Ministry of Employment is to tighten the use of detailed regulations and indicators in monitoring policy implementation, one outcome could be a more mechanical and standardised use of instruments than under the present system.

A final challenge for the new system is to engage the social partners in the implementation of labour market policy. This engagement has, under the present system, been supported by the fact that the

participants in the tripartite bodies at the regional level had a major influence over the allocation of economic resources for active measures. Given that this is no longer the case, one can question the enthusiasm with which the social partners will engage themselves in the new system of governance. There is a danger that their positive engagement will turn into negative criticism of activities over which, they have had little or no influence.

#### 4.1.3 THE PRACTICAL IMPLEMENTATION OF THE REFORM<sup>9</sup>

At the local and regional level, 2006 will be a year of transition from the old to the new structure – not only with respect to labour market policy, but for local and regional administrative and political bodies in general.

During the first half of 2005, the National Labour Market Authority [*Arbejdsmarkedsstyrelsen*] has had a dialogue with the municipalities concerning the establishment of the job centres. In the fall of 2005, this dialogue take place between the municipalities and the now appointed new “employment directors” of the four regions.<sup>10</sup> During the first quarter of 2006 the ten pilot job centres will be appointed. Also during 2006 the new job centres will be established in all municipalities and ready to start work on January 1, 2007. Also procedures for transferring the (unemployed) jobseekers to the new system have been outlined.

The rather complicated nature of this process (included the need for “dialogue” between the different levels) is of course partly due to the political autonomy of the Danish municipalities, which under the legislation have a high degree of self-governance.<sup>11</sup>

As mentioned above, the reorganisation of labour market policy will from 2007 imply the establishment of joint local “job centres” integrating the activities of the municipalities and the Public Employment Service. Hitherto the division of labour has been that the municipalities have been responsible for the unemployed, who were not members of an unemployment insurance fund, while the PES has taken care of the insured unemployed. Now a more integrated system will be introduced. The exact organisation of the “job centres” has been the cause of some political turmoil. A model has now been chosen, where the vast majority of municipalities will have a job centre,

<sup>9</sup> On the homepage of the National Labour Market Authority, a detailed description of this process can be found (<http://www.ams.dk/jobcenterguide/Proces/>)

<sup>10</sup> The “employment directors” (*beskæftigelseschefer*) is a new category of civil servants responsible for the practical implementation and management of the state tier of the new regional and local system. At the regional level, four “regional directors” (*regionsdirektører*) will also be appointed. Their role will be of a more strategic nature, although the exact division of tasks between the two types of “directors” is not entirely clear-cut.

<sup>11</sup> For a brief exposition in English of the extent of self-governance in Denmark, reference can be made to the homepage of the organisation Local Government Denmark (<http://www.kl.dk/296095/>)

which is still two-tier in its organisation. The care for the insured unemployed will be in the hands of a state-run section of the job centre, while the non-insured unemployed will be handled by a section under control of local government.

Only in about ten regions a truly integrated job centre will be established (as a pilot-scheme) with all unemployed being under the auspices of the local government (the municipality). Not surprisingly, this mixed system of governance has given rise to some criticism and fear of huge implementation problems.

#### **4.1.4 THE IMPORTANT ROLE OF THE NATIONAL ORGANISATIONS OF REGIONAL AND LOCAL GOVERNMENT**

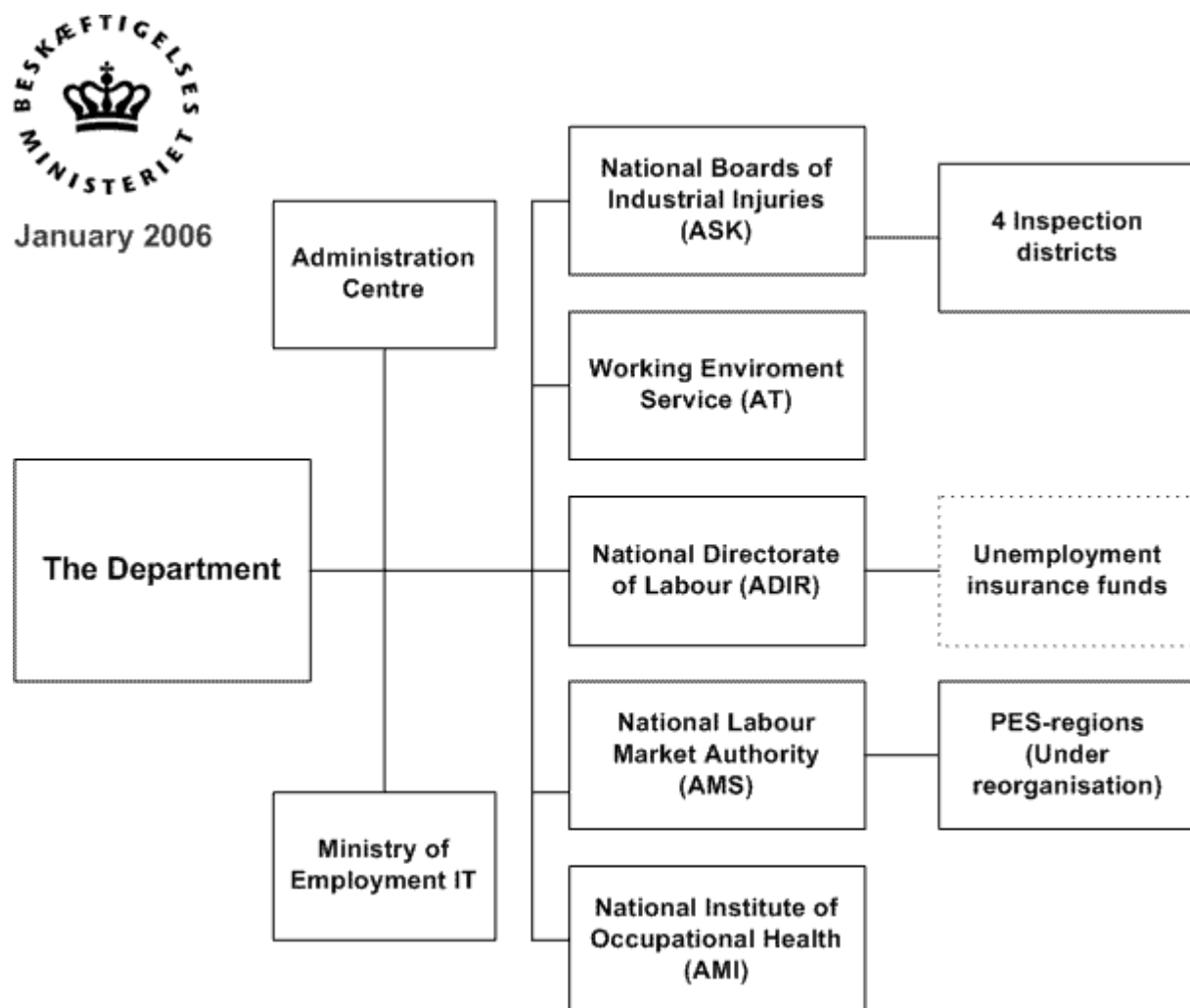
The autonomy of local government is reflected in the fact that both the regions and the municipalities have their own national organisations (Danish Regions [*Amtsrådsforeningen*] and Local Government Denmark [*Kommunernes Landsforening*]). Both organisations play a key role, when tasks and resources are allocated between the different levels of government for instance during the yearly negotiations on the state budget. The two organisations are also actively involved in preparing the National Action Plans for Employment (NAPs).

One should furthermore note that when it comes to labour market and employment policy, the two organisations are seen as much as representative of “social partners” as of the local and regional level. This is due to the fact that they are both large employers. Together they employ almost 700,000 persons equal to more than 25 percent of total employment. The 275 Danish municipalities alone employ almost 500,000 persons. In many local areas they constitute the largest employer.

## **4.2 DISTRIBUTION OF RESPONSIBILITIES**

Given the complex governance system found on the Danish labour market with a mix of legislative regulation (including implementation of EU-regulations) and regulation through agreements between the social partners, it is hard to define precisely the relation between the responsible institutions of active labour market policy. Important elements in the system of responsible institutions can however be identified by studying Figure 4.1.

Figure 4.1: The organisational structure of the Ministry of Employment



The diagram shows the internal administrative structure of the Ministry of Employment as of 2006. Of main interest in the present context are the National Directorate of Labour and the National Labour Market Authority. The former is responsible for the unemployment insurance funds and also (not shown) for the economic support from the municipalities to the non-insured unemployed. The latter is responsible for the operation of the Public Employment Service and (from 2007) for the new integrated job centres in the municipalities.

Not shown in the diagram are the corporatist bodies at national, regional and local level. Most of their names and tasks will change with the reform implemented in 2006-2007, cf. Table 4.1 below.

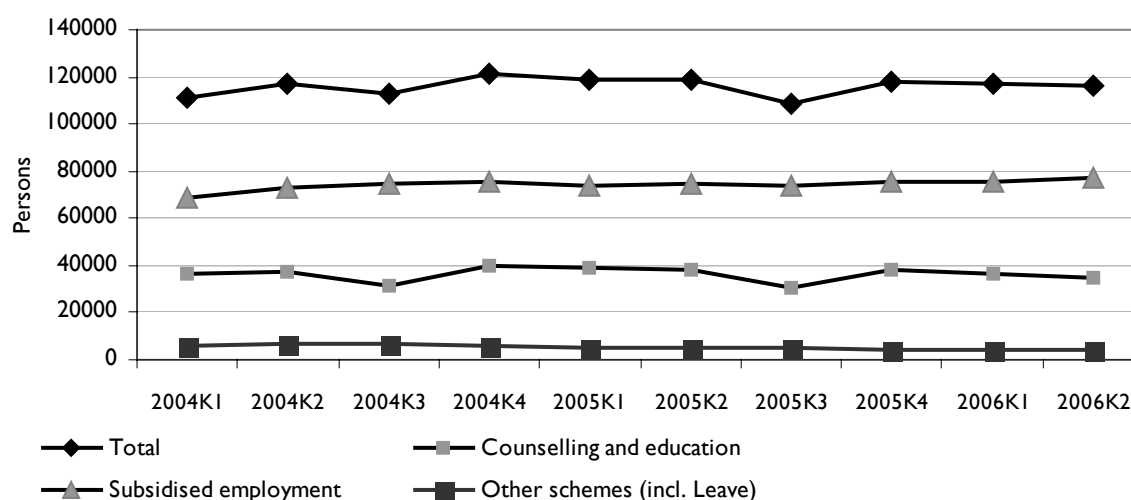
Table 4.1: Corporatist bodies at national, regional and local level before and after January 1, 2007

Level	Until 2007		From 2007 and onward	
	Name	Main tasks	Name	Main tasks
National	National employment council	Advisory body to the Minister of Employment	National employment council	Advisory body to the Minister of Employment
Regional	Regional labour market council	Implementing active labour market policy with substantial own funds	Regional employment council	Advising the regional labour market director. Monitoring regional labour markets.
Local	Local coordination committees	Advising the municipality	Local employment council	Advising the municipality

### 4.3 PARTICIPANTS IN ACTIVE LABOUR MARKET POLICY

The total number of participants in programmes of active labour market policy (including leave schemes) was 117,700 people in the fourth quarter of 2005, which represents a minor decrease from the peak level of 121,300 people in the fourth quarter of 2004 (see Figure 4.1). However, the total number has been surprisingly stable over the last two years, in spite of the strong decline in open unemployment. This has – not surprisingly – stimulated debates about the extent to which active labour market programmes are effective in getting the participants back into employment. The stable number of persons in subsidised employment hides a continued increase of the number of persons in “flexi-jobs”, which are jobs for persons with a permanent reduction in their employability. These kinds of jobs are increasingly used as an alternative to invalidity pensions.

Figure 4.2: Number of participants (full-time equivalents) in active labour market policy measures, first quarter of 2004 to fourth quarter of 2005.



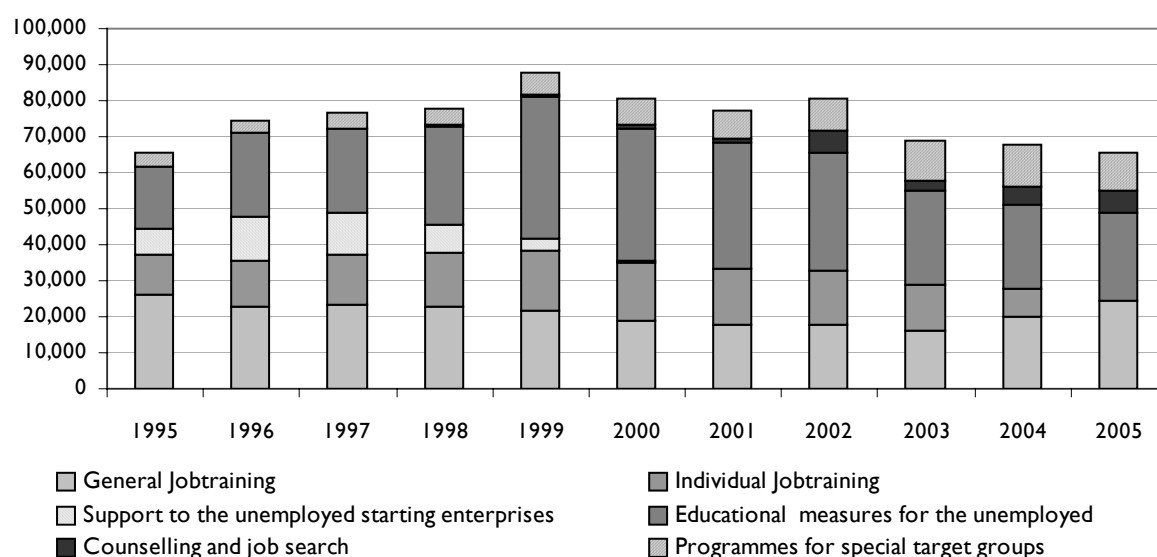
Note: “Leave” mentioned under other schemes is the old parental leave scheme introduced in 1993, which is currently being phased out.

Source: Databanks of Statistics Denmark.

Figure 4.2 shows the participants in active labour market policy the period 1995-2005 (excluding participants in flexi-jobs). The Figure has information about the main programmes of Danish active labour market policy:

- Job training with a wage subsidy implies that the unemployed is paid a normal wage from a public or private employer for a limited time period (up to one year).
- Special job training is for weaker groups of unemployed and will typically take place in special projects in the public sector.
- Support to self employment (a three year subsidy equal to 50 percent of benefits) was phased out from 1998. The programme is now closed.
- Education covers a wide range of education and labour market training with a duration up to one year.
- Counselling includes job search activities etc.
- Targeted measures are programmes targeted at special groups like immigrants or older worker.

Figure 4.3: Number of participants (full-time equivalents) in active labour market policy by type of measure, 1995-2005.



Source: Databanks of Statistics Denmark.

Mainly as a reflection of the improved conditions on the Danish labour market the number of participants has been falling in recent years. At the same time – and reflecting a deliberate policy shift of the present government – more emphasis has been put on job-training with private employers and on counselling under the heading “work-first”. Lower priority is given to educational measures. Also targeted measures have grown in importance due to the increased emphasis on the integration of immigrants and descendants.



## 5 PERFORMANCE

### 5.1 LABOUR MARKET INTEGRATION OF DIFFERENT GROUPS

Looking at the level of labour market integration measured by employment and unemployment rates, Table 5.1 presents some of the main observations.

Table 5.1: Key indicators on labour market integration in Denmark and EU-15, 2003

	Denmark Percent	EU-15
Employment rates:		
All age groups 15-64 years	75.1	64.3
15-24 years	59.6	39.7
24-54 years	83.5	77.2
54-64 years	60.2	41.7
Part time employment rate	21.3	18.6
Unemployment rate	5.6	8.1
Youth unemployment (as share of total population aged 15-24 years)	6.8	7.3
Long term unemployment	1.1	3.3

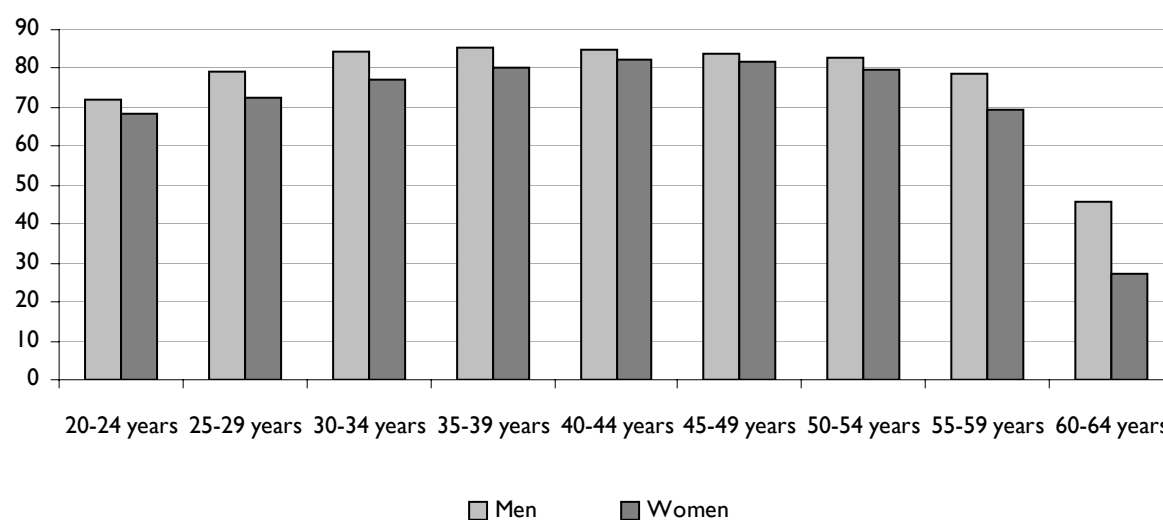
Source: LFS-data from European Commission, 2004, statistical annex.

The table reveals the well-known characteristics of the Danish labour market, when compared to the rest of the EU: a high employment rate and a low unemployment rate, also when it comes to long-term unemployment. One notes the very high employment rate for young persons, which reflects mainly the widespread habit of combining study and work. Part-time rate is a little above average due to the rather high level of female employment combined with the fact that more women are working part-time.

Concerning employment rates, one of the characteristic aspects of the Danish labour market is the high employment rate for both men and women in all age groups, cf. Figure 5.1.12. Thus, the female employment rates are almost equal to those of males, except for the age groups between 25 and 34 years, where caring for small children is reflected in a somewhat lower employment rate. In a comparative perspective one may add, however, that the employment rates for Danish women are among the highest in the European Union, also when it comes to women with small children (Eurostat, 2005).

<sup>12</sup> The definition of employed persons in Figure 5.1 includes persons employed with a wage subsidy, but excludes persons on leave (for instance on maternity leave) and persons receiving public sickness benefits.

Figure 5.1: Employment rates for men and women by age (percentage of labour force), 2004.

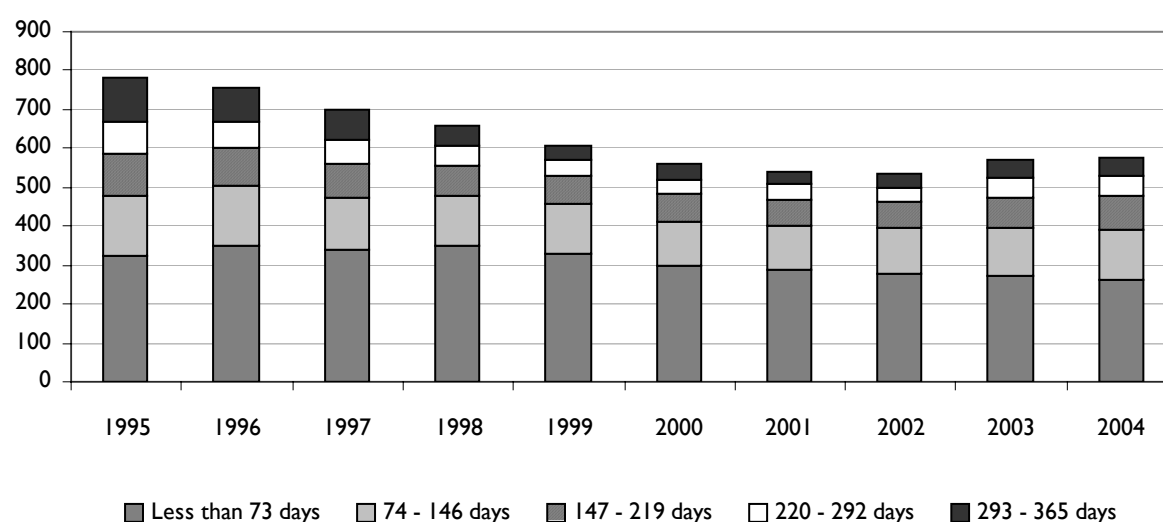


Source: Databank of Statistics Denmark

## 5.2 UNEMPLOYMENT FLOWS AND RATES

One of the characteristic features of the Danish labour market is the high volume of flows in and out of unemployment. Figure 5.2 shows the number of persons having been unemployed for a shorter or longer period of time in each of the years from 1995 to 2004.

Figure 5.2: Number of persons having been unemployed by unemployment duration (x 1,000), 1995-2004.



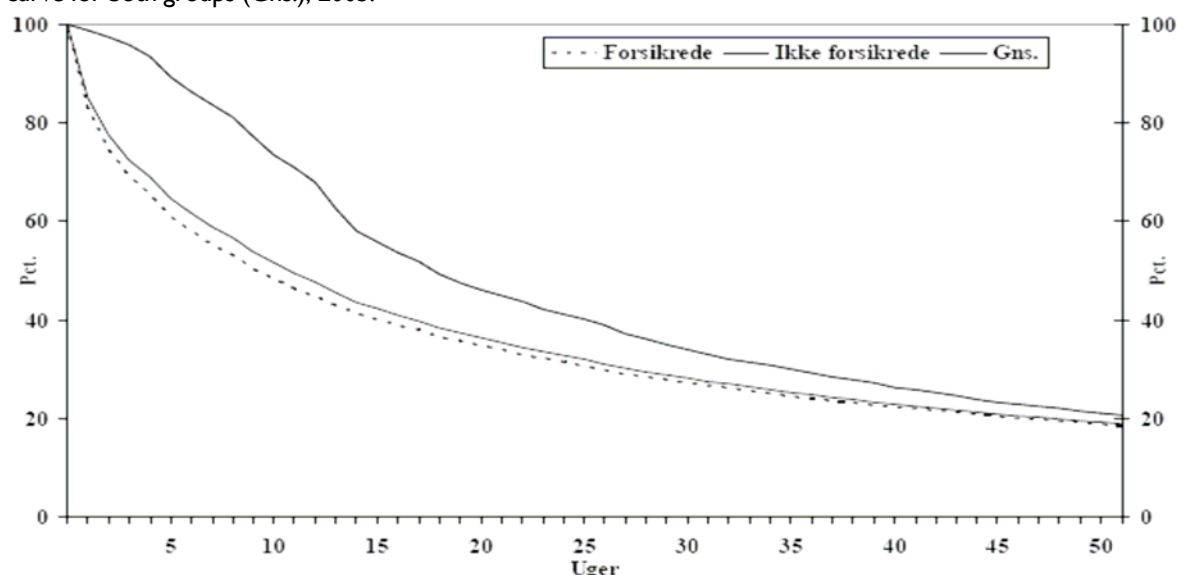
Source: Databank of Statistics Denmark

In 1995 a total of nearly 800,000 persons or almost one third of the workforce was unemployed one or more times during the year. About 323,000 experienced unemployment less than 20 percent of the year, while 114,000 persons were unemployed for more than 80 percent of the year, and thus

considered long-term unemployed by the standard definition applied in Danish statistics.<sup>13</sup> The graph illustrates the reduction in the number of persons experiencing unemployment during the upswing of the 1990s and the slight increase in 2003 and 2004. From 2005 the numbers are falling again. The number of long-term unemployed has been falling from more than 100,000 persons in the beginning of the period to less than 50,000 persons in the most recent years. These figures can be compared to a total workforce of 2,895,950 persons in 1995 and 2,854,100 in 2004.

The dominance of short term unemployment on the Danish labour market is also illustrated in the survival curve (Figure 5.3), which shows the outflow from unemployment to employment (including state-supported education) or retirement for the 130,000 new unemployed entering unemployment in the period from the 3<sup>rd</sup> quarter of 2002 to the 2<sup>nd</sup> quarter of 2003. After 6 months about 68 percent were in employment, while 80 percent were in employment after one year (Beskæftigelsesministeriet, 2005a). The curve also shows the difference between the insured and the non-insured unemployed. The latter has a lower outflow from unemployment in the first weeks of unemployment, but after a year the share left in unemployment is about the same for the two groups.

Figure 5.3: Survival curves for insured (Forsikrede) and non-insured (Ikke forsikrede) unemployed and average curve for both groups (Gns.), 2005.

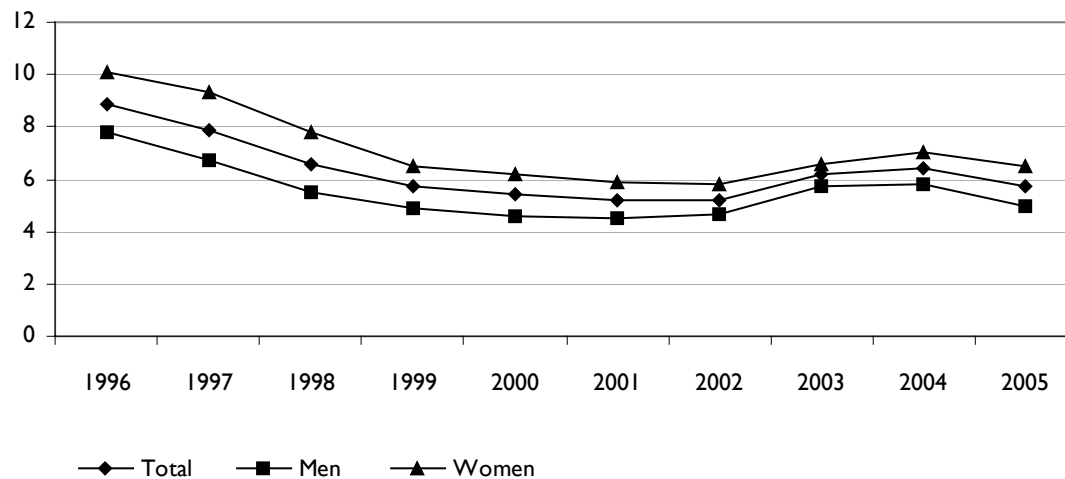


Source: Beskæftigelsesministeriet 2005a, Figure 2.

<sup>13</sup> The most important statistical concept in Danish unemployment statistics is the “degree of unemployment”, measuring the percentage of a year in which a person has been registered as unemployed. A long-term unemployed is defined by this measure as a person having been unemployed for more than 80 percent of a given year. This definition differs from the concept applied in the labour force survey, where a person is considered unemployed if s/he has been unemployed for more than 12 months.

The unemployment rate by sex is shown in Figure 5.4, which documents the somewhat higher unemployment for women than for men. Thus in 2005 the average unemployment rate for men was 5.0 percent and for women 6.5 percent.

Figure 5.4: Unemployment rate for women and men (% of labour force), 1996-2005.

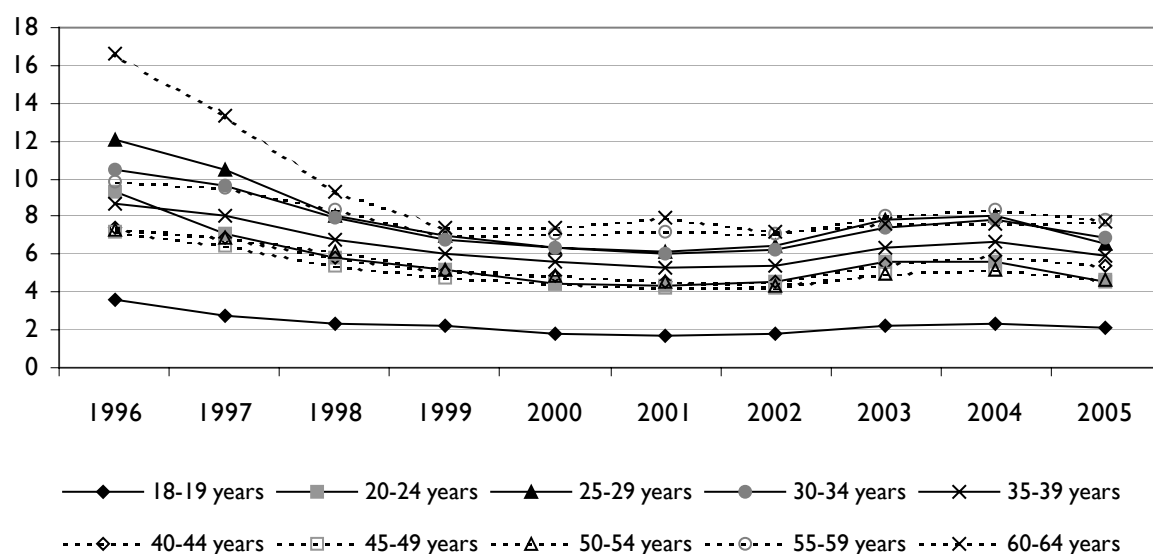


Source: Databank of Statistics Denmark

Similarly the unemployment rates for different age groups are documented in Figure 5.5. The relationship between the age groups is rather stable. In 2005, unemployment rates above 6 percent are found for the age groups 24-34 years and for those aged 55 years and more. A remarkable feature of the Danish labour market is the low youth unemployment rate, which is often attributed to the special youth measures introduced in 1996. The overall purpose of the youth programme was to stimulate unemployed, low-skilled youngsters to take up paid employment or to participate in education.

Originally, the programme was only targeted at young people under the age of 25 who have not acquired professional or vocational qualifications and who are entitled to regular unemployment benefits. But as a result of the success of the scheme, the youth package was since January 1999 extended to cover all persons under the age of 25 claiming regular unemployment benefits. The main aim of the programme is to motivate young unemployed to undertake ordinary education or to find an ordinary job on their own initiative. If they fail to do so within six months of unemployment, they have the right and duty to participate in full-time special vocational education or training (in ordinary education or in other activities, such as job training) for at least 18 months received a benefit, which is fifty percent of the normal. It is however disputed, whether the lowering of the rate of youth unemployment is also due to other factors including the general economic upswing since the early 1990s (see Bredgaard & Jørgensen, 2000).

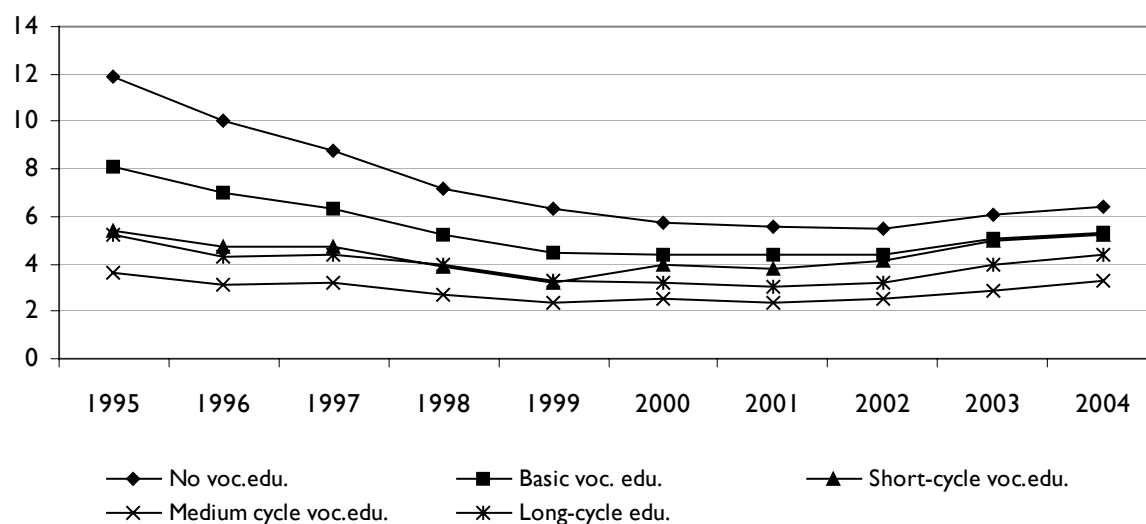
Figure 5.5: Unemployment rate for different age groups (% of labour force), 1996-2005.



Source: Databank of Statistics Denmark

Another important factor related to the unemployment rate is the educational background, which is of course also to some degree correlated with age and sex. As shown in Figure 5.6 there is a stable hierarchy, where the highest unemployment rates are found for those groups without any vocational education and the lowest for those with a medium-cycle vocational background.

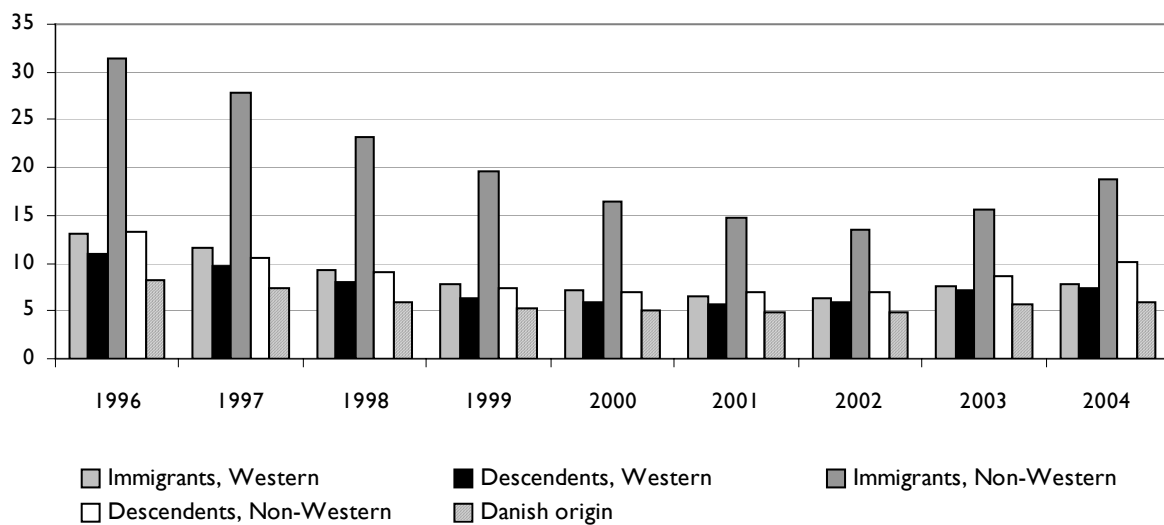
Figure 5.6: Unemployment rate for different educational groups (% of labour force), 1995-2004.



Source: Statistical Ten-year Survey 2005, Statistics Denmark

An important issue of the Danish labour market is the difficult employment situation of immigrants from non-Western countries, which is also illustrated by the unemployment rates in Figure 5.7. Especially first generation immigrants stand out as having very high unemployment rates.

Figure 5.7: Unemployment rate for different ethnic groups (% of labour force), 1996-2004.



Source: Databank of Statistics Denmark

Several interrelated reasons can be pointed to in explaining the barriers that immigrants and descendants from non-western countries meet on the Danish labour market:

- Their lower average level of education;
- Language barriers;
- Discrimination;
- The narrow wage dispersion, which makes it difficult for persons with a very low productivity to enter into employment (e.g. unskilled immigrants with insufficient language skills);
- Unemployment traps due to relatively high social benefits (although special low level has been introduced for some immigrant groups); and
- The fact that many non-Western immigrants seek to Denmark for other reasons than to find a job (political asylum or family reunification).

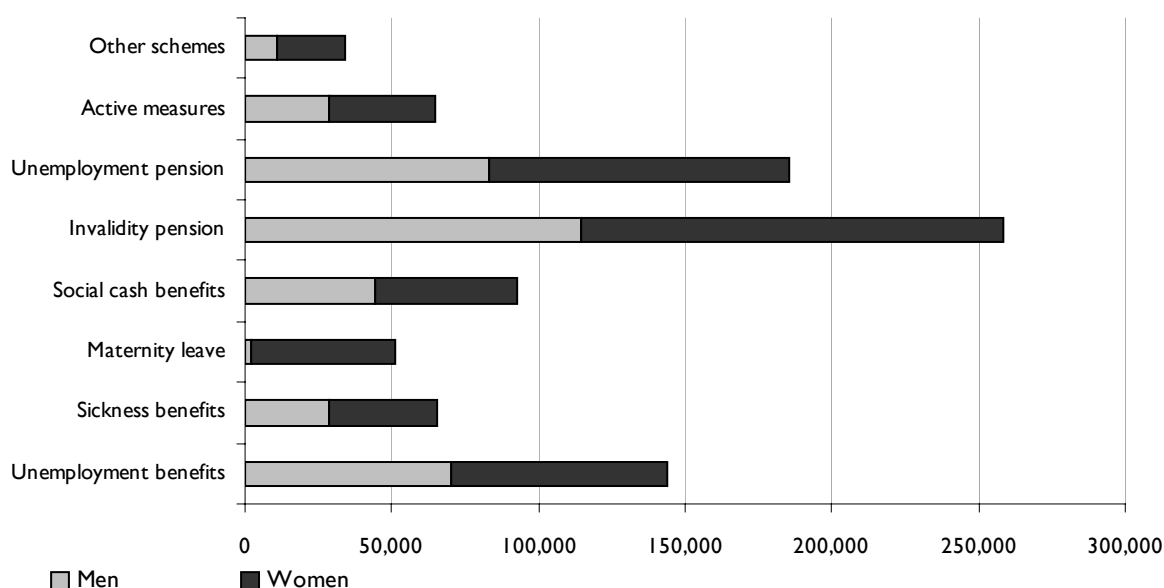
While the former three barriers will be valid for most European countries, the three latter are probably more dominant on the Danish labour market than in many other Central or Southern European countries.

### 5.3 THE ECONOMICALLY INACTIVE

Turning to the issue of the economically inactive, the number of registered unemployed presented above tells only part of the story about how many adults, which are economically inactive. As indicated by Figure 5.8, the number of unemployed in 2004 was surpassed by both the number of recipients and invalidity pension and the number of persons receiving Voluntary Early Retirement

Pay (Unemployment pension). This scheme under certain conditions allows persons aged 60-65 years to retire and receive a pension equal to unemployment benefits. The total number of persons receiving some form of transfer income in 2004 was almost 900,000 persons (full time equivalents) or about 25 percent of the adult population aged 15-65 years. Given the fact that the average employment rate in the same year was almost 75 percent, the striking observation is that for adult Danes there are only two alternative positions vis-à-vis the labour market: either as employed or as recipient of public transfer income.

Figure 5.8: Number of adults (aged 15-65 years) receiving some form of transfer income, full time equivalents, 2004.



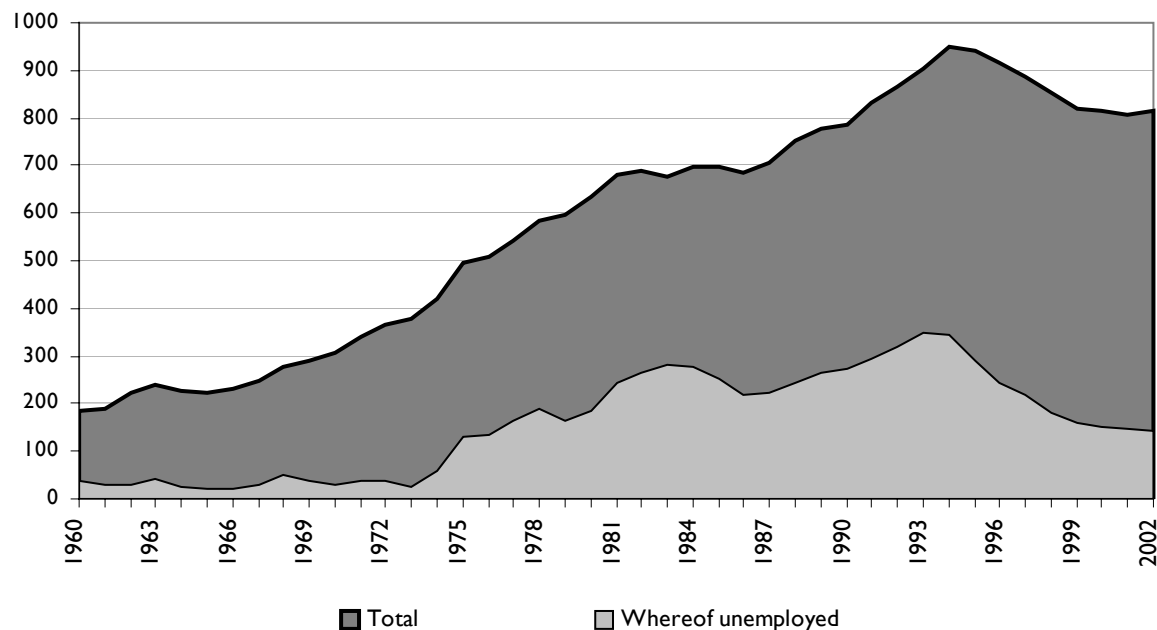
Source: Databanks of Statistics Denmark

As indicated by the time-series in Figure 5.9, the number of persons receiving some form of public transfer income has increased rather dramatically since the early 1960s. The number reached a peak in the mid-1990s and then declined a bit as a reflection of the improved situation on the labour market and, perhaps, also more efficient policies.

Figure 5.9 might leave the impression of an employment system under considerable strain. However, the data in Figure 5.10 indicates that the picture is more mixed. When looking at the distribution of the adult population by activity-status from 1960 to 2002, the remarkable observation is that the share in employment has been rather stable at the level of about 75 percent – thus indicating that an employment rate of the magnitude is a stylised fact of the Danish employment system. Within the group of employed, one observes an increase in the share of public employees during the 1960s and 1970s as a reflection of the development of the modern Danish welfare states. The most dramatic change, however, has taken place among the economically inactive. Here the group of adult persons

not receiving an income from employment or from the public sector (mostly women working at home) has almost vanished. Instead one sees the steep growth in the groups of persons receiving public transfer income.

Figure 5.9: Adults receiving transfer income (full time equivalents, x1,000), 1960-2002.

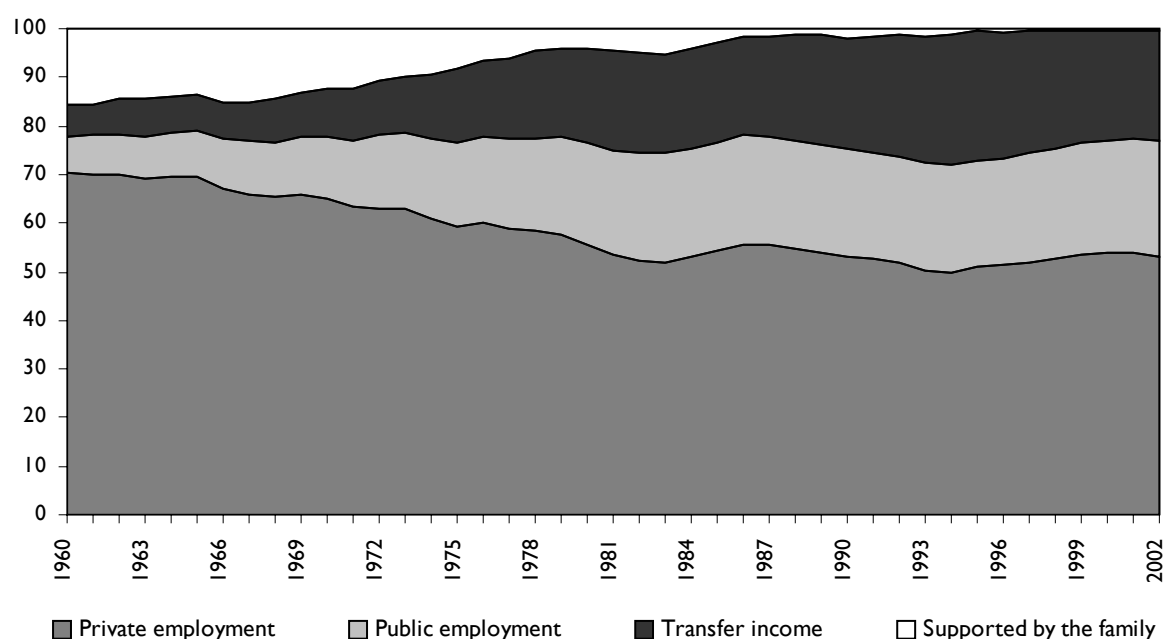


Source: Author's calculations based on data from the Ministry of Finance and Databanks of Statistics Denmark.

The fascinating thing about Figure 5.10 is that it – in one glimpse – tells the main story about the interplay between the labour market and the welfare state in Denmark over the last four decades. Thus the abolishment of the housewife marked the end of the traditional male breadwinner family and the full integration of the women into the labour market, many as public employees with healthcare and social services. The figure also shows the strong processes of marginalisation on a labour market characterised by rapid technological change and high demands on productivity associated with high average wages and rather narrow wage dispersion. In a situation where economic safety nets are available, and for some groups even attractive compared to earned income, it is not surprising that the number of inactive recipients of transfer income grew at a quick pace – and often most rapidly in periods of economic decline.

The previous analysis has focused on the developments of net stocks over time and thus provided limited information about the flows of persons between different situations in the labour market. Due to the availability of administrative registers, it is possible to trace the labour market attachment of individuals over time. The Economic Council published one such study in 2000 looking at the shift between different positions vis-à-vis the labour market based on a core-periphery-scale.

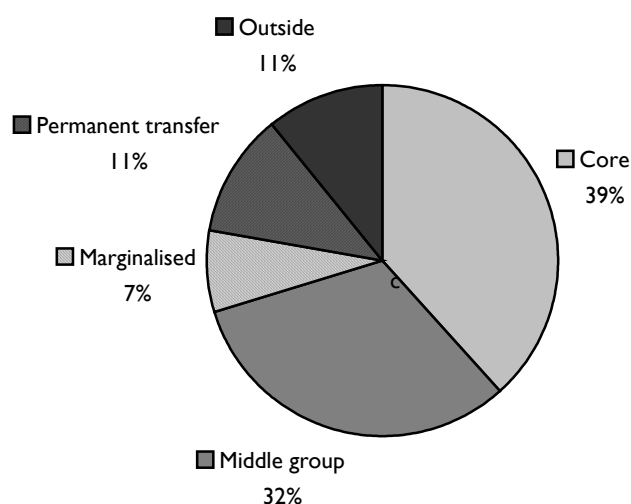
Figure 5.10: Adult population aged 15-65 years by activity-status, 1960-2002.



Source: Author's calculations based on data from the Ministry of Finance and Databanks of Statistics Denmark.

Figure 5.11 shows the distribution of the adult population aged 15-65 years by their dominant labour market status in the period 1995-1997.

Figure 5.11: Population aged 15-65 by dominant labour market status 1995-1997.



Source: Author's calculations based on Det økonomiske Råd (2000), Table III.1

As shown in Figure 5.11, about 39 percent of the adult persons have full time employment and rarely experience unemployment. They are therefore labelled the "core". Almost as many (32 percent) have a more unstable employment career ("the middle group"), but are still predominantly employed. The group of "marginalised" persons (here defined as persons being unemployed for

more than 80 percent of the time incl. recipients of social benefits not registered as unemployed), the persons permanently on transfer income and persons outside the labour add up to a total of 29 percent of the adults.

However, the statuses in Figure 5.11 are not permanent, when you look at the individual labour market careers. The Table below indicates the dynamics involved.

Table 5.2: Labour market status in 1995-1997 by status in 1992-1994.

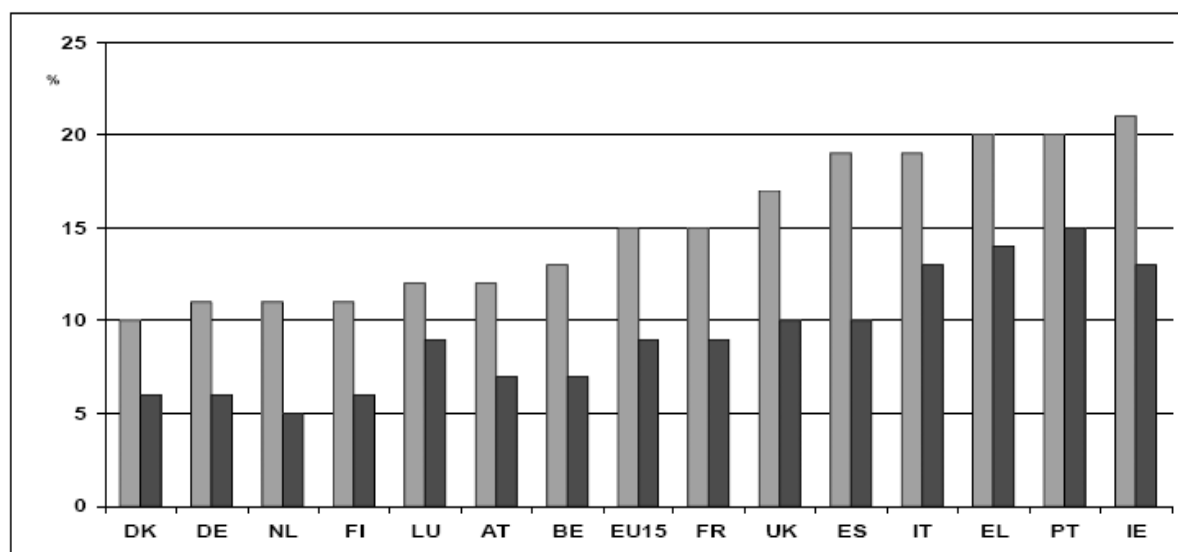
Status 1992-94	Core	Part-time	Middle group	Marginalised	Social security	Permanent transfer	Outside workforce	In education	Dead	Total
Core	75,1	2,4	13,1	0,3	1,3	4,4	1	1	1,2	99,8
Part-time	21,5	35,6	27,1	0,6	2,3	7,1	2	2,3	1,3	99,8
Middle group	32,9	4,1	38	4,5	5,1	5,6	1,6	6,5	1,7	100
Marginal	2,8	0,4	38,4	20	9	20,4	1,7	5,9	1,9	100,5
Social security	6,9	2	32,4	3,6	25,8	16,3	3,6	5,7	3,6	99,9
Permanent transfer	0	0	0,1	0	0,3	93,2	0,3	0	6	99,9
Outside workforce	16,1	4,6	15,6	0,6	3,4	12,2	35	3,6	8,7	99,8
In education	8,2	1,8	45,4	1,5	3,2	3,4	1,5	35,4	2,8	103,2

Source: Det økonomiske Råd, 2000, Table III.1

Thus, while there is for some groups (especially the core-group and the group on permanent transfer income) a clear tendency to stay in the same group from the first to the second period, other position are much more transient in nature. Thus for the members of the marginal group or the group on social security, around one third moves into the middle group, and thus gains a more stable foothold on the labour market. Also the group working part-time is highly mobile, shifting to positions either in the core or in the middle group.

A final comparative piece of evidence concerning the number of persons located “downstairs” in the Danish labour market model is shown in Figure 5.12, which shows the share of persons categorised as poor in 1996 and as persistent poor over a longer periods of time. Measured by both indicators, there is little evidence that the combination of low employment protection and income/employment security makes for high risks of becoming poor or permanently poor.

Figure 5.12: Persistent risk-of-poverty rate for 1998-2001 (right) and at-risk-of-poverty rate (left) for 2001 in Denmark and a number of other EU Member States.



Note: The risk of poverty rate measures the share of the population living in households with an “equivalised disposable income” below 60% of the median equivalised income of the country they live in. The persistent risk of poverty rates measures the share of the population that in in risk of poverty in at least two out of the three preceding years.

Source: Eurostat (2004), Figure 5.

Summing up the picture of the different groups in the Danish labour market, the main groups of winners appear to be large groups of salaried workers, skilled workers and also some unskilled groups. On the other hand, the main groups of losers are indicated by the general growth in the number of adults receiving transfer incomes. This group may not all be in risk of absolute or relative poverty. But they will in many cases suffer from social exclusion due to the important role of working life as a road to social integration in Denmark. The groups mostly in risk of becoming marginalised are thus immigrants from non-Western countries, some unskilled groups, older workers and persons with health problems. However it is unclear, whether the Danish version of flexicurity in itself is the cause of these exclusionary elements in the Danish employment system. Thus one can argue that a lower level of employment protection has the role of creating winners also among the weaker groups on the labour market due to less statistical discrimination.

Furthermore, within the framework of the Danish model, active labour market policy and policies to support adult education and training has the role of improving the employability for those groups that are in danger of becoming marginalised. One may see these institutional arrangements also as counterbalancing the risk of firms providing less continued education and training to their employees, due to the risk of losing their human capital investments with employees leaving their jobs.

## 5.4 EFFECTS OF ACTIVE LABOUR MARKET POLICY

As in many other countries, the net effects of active labour market policy are disputed. One reason is that active programmes have both positive and negative effects on the future employments prospects of the individual participants:

- The *motivation effect* implies that an unemployed person seeks work more actively in the period immediately *before* she or he has to participate in a mandatory activation programme. The strength of the motivation effect is indicated by the change in the probability of leaving unemployment in the period immediately before the person is obliged to take part in an activation programme.
- The “*locking-in*”-effect means that job-search activities are reduced during the period that an individual takes part in a programme.
- The *training (or qualification) effect* stems from the rise in the level of qualifications during activation, which should improve the possibilities of finding a job for those who have participated in one of the active programmes.

In a study published in 2000, the Ministry of Labour presented some of the first results based on a new database, which it had developed (Ministry of Labour, 2000). The database contains information on the labour market situation of all individuals, including their participation in labour market programmes and their contacts with the social security system.

First of all, the study revealed significant motivation effects, measured by an increased probability to take up employment in the period immediately before having to take part in mandatory activation programmes. Such effects have been confirmed by later studies (e.g. Geerdsen, 2003; Rosholm & Svarer, 2004) and play an increasing role for the proponents of active programmes. However, the specific dilemma posed by such observations should be borne in mind. If it is wished to increase the motivation effect, there may be a temptation to change the content of activation programmes in order to make them less attractive to participants. But this would also probably imply that the *quality* of the programmes themselves would be lowered in terms of their training content and other activities to improve the skills of the participants. As a result, the overall outcome might be less positive for those unemployed persons who are unable to find a job before entering activation.

Another potential effect for the individuals taking part in activation programmes is that they increase their chance of gaining employment due to the improvement in their qualifications and therefore their employability. In the study by the Ministry of Labour, the improvement in employability is measured by the reduction in the proportion of the year for which the persons concerned receive

any form of transfer income (such as unemployment benefit, social assistance or sickness benefit). A reduction in this proportion is a reliable indicator of a genuine improvement in the employment situation of an individual, either because they have found ordinary employment or taken up some form of ordinary education.

#### **5.4.1 ESTIMATION OF THE DIFFERENT EFFECTS**

Such qualification effects of the various types of labour market programmes are of considerable interest. In this respect, the largest improvement in the employment situation (measured by an increase in the economic self-dependency of the participant) was in the study from 2000 found for participants in private job training. For public job training and labour market education the effects are positive, but smaller. These findings are in line with international experience (Martin, 2000).

In the most recent study from the Ministry of Employment (Beskæftigelsesministeriet, 2005), the following conclusions are made concerning the qualifications effects:

- Positive effects from participation in active programmes are found for both insured and non-insured unemployed and the estimated magnitude of the effects are rather similar;
- Job training with a wage subsidy gives the largest effects, especially job training in the private sector;
- Positive effects are also found for educational programmes, especially when targeted towards job-types with labour shortages;
- Especially for non-insured unemployed one observes a larger effects of education, when measuring the effect one year after participation compared to measuring the effects after six months, thus pointing to the importance of longer term effects; and
- Finally it is observed that combinations of different programmes (for instance education combined with job-training) gives larger effects than just participating in single programmes, although this must also be seen in the light of the longer duration of such combined programmes.

Some studies have been sceptical towards the positive net effects of active programmes, often pointing to the existence of significant locking-in effects. By example, the Chairmen of the Economic Council in their report from December 2002 ascribe about one third of the reduction in unemployment since 1993 to improved structural performance of the Danish labour market and attributes part hereof to improved labour market policy (Det økonomiske Råds formandskab, 2002). However, the report gives a rather critical account of the majority of the instruments applied within active labour market policy and especially points to significant locking-in effects of several measures.

Only job training in private firms seems to have large positive net effects and to be cost-effective. Job-training in the public sector and many forms of education have dubious or negative net outcomes for the participants. On this background the Chairmen proposes improvements in the use of active measures (including giving higher priority to job search and private job-training).

#### **5.4.2 CREAMING AND PARKING**

One barrier to getting reliable quantitative assessments of the effects of different programmes is of course the heterogeneity of the participants. While easily observable differences between participants with respect to for instance age and education can be compensated for by well-known statistical techniques, it is more difficult to take account for unobserved differences like work motivation and self confidence. These problems will of course be reinforced, if those actors responsible for the programmes are able to discriminate between different participants based of their assessment of the degree to which they will benefit from the offers of the programme. Such effects are often referred to as *creaming* (preferential treatment of “strong” unemployed) and *parking* (giving the less resourceful unemployed only the minimum remedies).

The existence of such effects has over the years been documented in several Danish studies of active programmes. Given the increased emphasis in recent years on private service providers and economic incentives in the implementation of the programmes, there is of course a higher risk of such effects, which have been observed in other countries introducing similar systems (cf. Bredgaard *et al.*, 2005). The results from a new Danish study indicate that this is actually the case although the use of private service providers in the Danish has some special traits including (Bredgaard & Larsen, 2006):

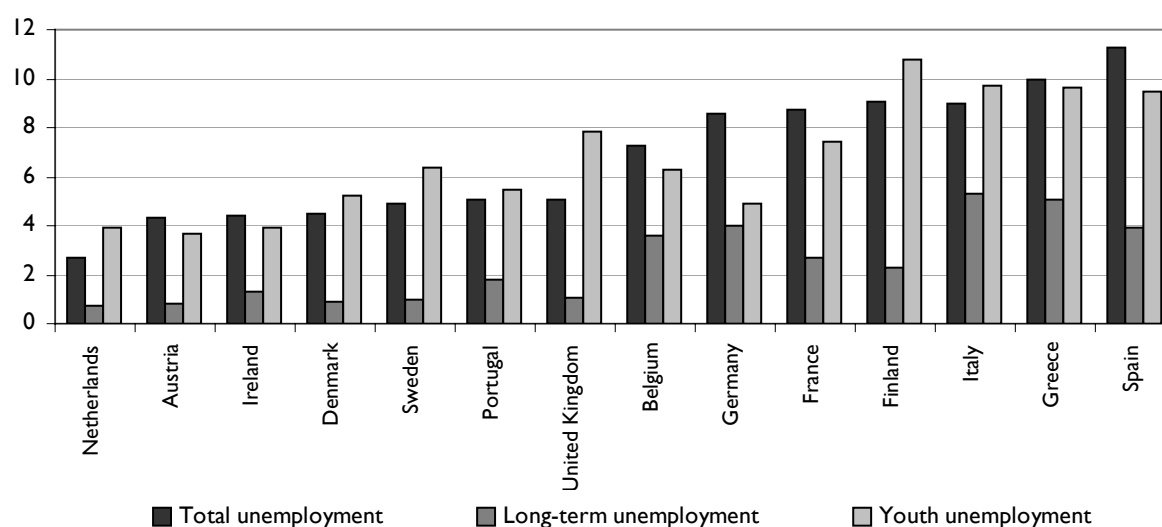
- Not applying a full-scale outsourcing but the parallel use of public, private and semi-private providers (including also some trade unions and unemployment insurance funds);
- A decentralised scheme for tendering;
- A process characterised by dialogue and cooperation between the PES and the service providers; and
- A inclusion of the social partners in the process of outsourcing (in some cases having the trade unions as providers).

#### **5.4.3 INTERNATIONAL COMPARISONS**

Concerning international comparisons, it is difficult to assess the efficiency of Danish active labour market policy in a comparative perspective. Figure 5.13 gives some data on overall unemployment,

long-term unemployment and youth unemployment for a number of European countries. As indicated by Figure 5.13, Denmark is among the best performers among the European countries, when assessed by various aspects of unemployment. Also when measured by other indicators of labour market performance like life-long learning, gender pay gaps, employment rates of older workers etc. Denmark is among the top performers of the EU Member States.

Figure 5.13: Total unemployment (unemployed as % of workforce), long-term unemployment (long-term unemployed as % of workforce) and youth unemployment (unemployed as % of age group) in a number of EU Member States, 2003.



Source: European Commission 2003, statistical annex. The countries are ranked according to the sum of the three indicators.

#### 5.4.4 MACRO-EFFECTS OF ACTIVE LABOUR MARKET POLICY

The evaluation findings discussed above have focussed on the micro-level. However, the coincidence of the implementation of the labour market reforms from 1993 and onwards and the dramatic fall in Danish unemployment during the 1990s has of course stimulated discussions about the extent to which the inflation-free macro-economic upturn can be attributed to the shift in labour market policy in the 1990s. A lowering of the level of wage inflation for a given size of unemployment is taken as an indicator of greater flexibility in the functioning of the labour market.

Of course, there could be a number of factors behind these developments. The changing attitudes of the social partners could be important. Thus, in 1987 the social partners issued a joint declaration stating that they would take the overall macro-economic performance into consideration and therefore negotiate wage increases below the international wage inflation in order to improve the competitiveness of the Danish industry. This declaration has since laid the foundation for the general wage negotiations. From a theoretical perspective this explanation can be supported by the concept

of the “negotiated economy”, which sees Denmark as a prime example of a society, where a joint conception of the overall targets and constraints for macro-economic development has been established (Nielsen & Pedersen, 1991).

Furthermore, Danish wage negotiations have to an increasing degree been decentralised to the level of the individual firms. Thus, in the collective agreements covering the major part of the private sector, only 15 percent of the agreements had centrally negotiated wage rates in 2000. In 1989, the share was 34 percent. The share of agreements, which mentions no wage rate at all increased during the same period from 4 to 20 percent (Dansk Arbejdsgiverforening, 2003: Table 8.10). According to the well know Calmfors-Driffill-hypothesis, this development could also explain slower wage growth.

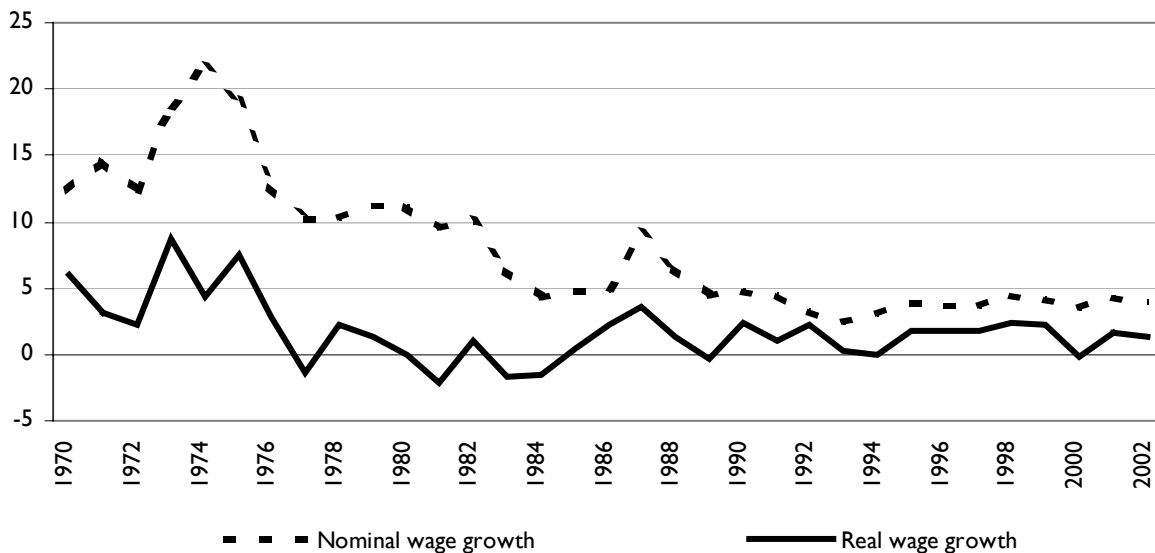
Combining the conditions for wage negotiations at the central and de-central level, one could therefore point to a shift in the norms for wage negotiations, which implies both a recommendation of wage restraint from actors at the central level and a higher acceptance of the need to keep wages in line with (foreign) competitors at the firm level. Thus shifts in norms and in the organisation of wage formation overruled the potential inflationary effects of a large reduction in unemployment. This points to the complexity of the forces that determine inflation and to the fragility of the traditional Phillips-curve.

In this context one must furthermore emphasize the lowering of the international level of inflation (including wage inflation) as an important factor behind the lower internal pressure for nominal wage increases. In their report from December 2002, the Chairmen of the Economic Council presented a new model of Danish wage formation, which includes wage increases abroad as an important explanatory variable. The estimate for the influence of foreign wage growth implies that Danish nominal wages increase by almost 0.6 percent, when foreign wages increase by 1 percent (Det Økonomiske Råds Formandsskab, 2002: pp. 155-6).

A final point worth taking into the argument concerning the lowering of nominal wage inflation is the difference between the development of nominal and real wages during the last decades, cf. Figure 5.14. The main message is that stable growth in real wages of about 2 percent per year can be reached also at a moderate level of nominal wage growth, as indicated by the experience from the 1990s. The opposite lesson was learned during the years from 1977 to 1986, where increases in nominal wages of 5 to 12 percent resulted in increases in real wages around zero. An added factor during the period from 1994 and onwards was the further increase in private consumption made possible by the growth in prices of private homes and the easy access to cheap mortgage. Therefore

the perception of the need to moderate nominal wage growth was strongly supported by the daily experience of the wage earners themselves – slow wage increases and rising living standards could easily go hand in hand.

Figure 5.14: Growth in nominal and real hourly wages for workers in manufacturing (in percent), 1980-2002.



Source: Databanks of the macro-econometric model ADAM (Statistics Denmark)

While one can therefore present a number of explanations for the shift in the unemployment-inflation nexus on the Danish labour market since the early 1990s, one can also point to evidence, which support the view that the *reforms of labour market policy* during the 1990s made a significant contribution to the improved functioning of the labour market. Thus the Chairmen of the Economic Council, who as indicated above are rather sceptical to the merits of active labour market programmes, nevertheless ascribe a little less than half of the reduction in unemployment since 1993 to improved structural performance of the Danish labour market and attributes a significant part hereof to the reforms of labour market policy, although they find it difficult to provide a more exact estimate. The Chairmen furthermore point to an increase in the share of unemployed that are actively looking for work and relate this to the shortenings of the period of passive benefits payments and the stricter demands to take part in activation (Det Økonomiske Råds Formandskab, 2002: pp. 163-5 and 153).

A study from the Danish National Institute of Social Research in 1998 summed up the evidence from a large-scale evaluation programme studying the initial labour market reform of 1994 (Larsen and Langager, 1998: pp. 34-36). Concerning the importance of the activation strategy, the analysis showed that:

- The employment goals specified in the individual action plans indicated that there was a *considerable planned mobility* among the unemployed;
- Labour market policy seemed to function effectively in that planned mobility among the unemployed was *larger* in those regions where the need for mobility was the highest (due to threats of bottlenecks);
- There were *significant positive employment effects* of both job training and education for unemployed; and
- The *effective supply of labour among the insured unemployed* seemed to have increased from 1994 to 1997 probably due to the stricter demands made on the unemployed during the second phase of the reform (for instance in relation to the increased demands on the young unemployed).

Concerning the activities directed at the firms, there were indications that the reform has contributed to the absence of bottlenecks since 1994:

- There was a (weak) indication that *the quality of the services of the Public Employment Service to the firms has improved* since the reform when looking at the ability to fulfil the needs for qualified labour (though there were also examples of labour shortages in the short run);
- The introduction of new forms of placement services (in the form of "open" self-service placements) had - together with the surveillance activities and regular contacts with employers - lead to *an increase in the transparency of the labour market* and thus improved its function as a system to match demand for and supply of labour; the market share of the Public Employment Service however, was still rather low.

Thus, based on the positive evaluation findings for both the process and the effect of the labour market reforms, there is a well-based case for arguing that the change in Danish labour market policy in 1993-94 has made a separate contribution to the improved functionality of the Danish labour market in recent years. The absence of labour shortages and wage-pressure since 1994, in spite of the fall in unemployment and the strong growth in employment, indicate that the functioning of the labour market has improved.

Also, as indicated in Figure 5.9 above, the number of both unemployed and the total number of adult persons receiving transfer income has been falling since 1993. The number of recipients of transfer income has been steadily rising since the early 1960s, but started falling in 1993. To what extent this is due to the labour market reforms, the economic upswing or to other of the above mentioned factors cannot be definitively determined on the basis of the available evidence.

## **5.5 INCENTIVES AND DISINCENTIVES FOR THE UNEMPLOYED**

The (lack of) economic incentives to return to employment due to the rather high levels of benefits, especially for those at the lower income levels, is a standing debate among both researchers and policy makers. A huge literature can be found concerning the assessment of the various incentives and disincentives. Only a few recent studies are mentioned below.

First of all one should notice that from the perspective of the flexicurity approach in the Danish case, the potential disincentives deriving from high income replacement rates of the UI-system are addressed by requiring the unemployed to be actively seeking jobs and by offering mandatory full-time activation after 12 months of unemployment for adults and six months of unemployment for young unemployed persons under the age of 25. Activation is therefore seen as fulfilling both a qualification and a motivational purpose.

Secondly, the standard view of labour economists is to express some worries about the disincentives of unemployment benefits. A characteristic example is the study by Pedersen and Smith (2002). Their results indicate large disincentive effects for some groups, especially low paid women. In 1996, 6 per cent of Danish men and 13 per cent of the women had a lower disposable net income if working in a full-time job compared to being on unemployment benefits. They find that the net compensation rate in unemployment has a significant impact on women's propensity to leave the labour force, on measures of search intensity, on the risk of being affected by unemployment, and on one of their flexibility measures, *i.e.* the maximum acceptable commuting time to a job. The net compensation rate has no impact on the willingness to move to another place to get a job. Also, the authors find a number of significant effects from attitude variables. However, the main conclusion is that economic incentives dominate the present analysis of unemployment traps.

Along similar lines, the Ministry of Finance in 2004 published a report on the role of taxation and other economic incentives (Finansministeriet, 2004). Among their main conclusions with respect to unemployment traps were that:

In general there are considerable economic incentives to become employed instead unemployed; thus the average net rate of compensation in 2004 was 63 percent (measured on the basis of disposable income). This represents a decline from 65 percent in 2001. The share of the employed persons for which the increase in disposable income is less than 1000 DKK per month was 5.4 percent in 2004, down from 7.8 percent in 2001.

While both these sources point to risks of unemployment traps at least for the lower income groups, other research has argued that such risks are negligible, mainly due to the fact that non-economic incentives combined with the availability of jobs play the dominant role, when explaining, whether unemployed return to work or not (Goul Andersen *et al.*, 2003).

## 5.6 WAGES AND SOCIAL INSURANCE

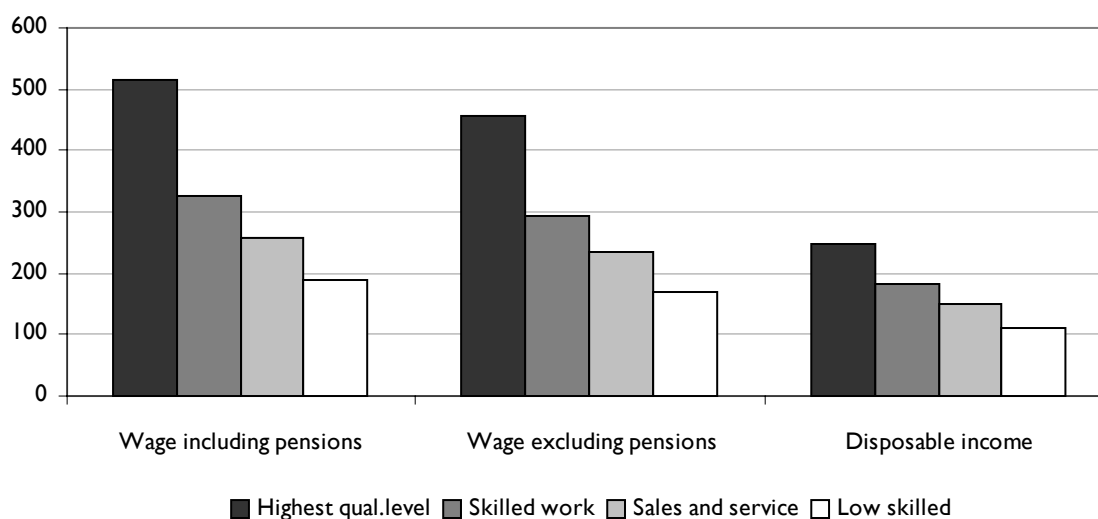
Over the last decade, wage setting in Denmark has become still more decentralised. Thus in 2004, only 16 percent of the collective agreements (measured by share of workers covered) under the DA/LO-area specified a standard wage rate (so-called “normal wage”). In 62 percent of the agreements, a minimum wage was specified, but actual wages were to be set by local negotiations. Finally in 22 percent of the agreements, no wage rate was mentioned at all. The latter represents an increase in such “wage-less” agreements from 4 percent in 1999. There is no statutory minimum wage in Denmark.

There are no formal links between wage setting and social insurance. Concerning informal interrelations, they are probably weak if existing at all. The reason is of course that neither the trade unions nor the unemployment insurance funds will experience any immediate costs, if excessive wage claims should cause increases in unemployment. This is of course due to the fact that the state pays for any increases in expenditures on unemployment benefits. One could add that economic experts from time to time have argued the case for making trade unions more responsible for the (assumed) consequences of wage increases by creating some connection between the memberships financing of unemployment benefits and the actual unemployment level, but without success.

Concerning wage levels and wage dispersion, Figure 5.15 gives a few basic facts. The largest dispersion is found for gross wages, where the relation between the highest and the lowest level is 2.7. For disposable income the relation is 2.2. Apart from this rather narrow wage dispersion, the Danish labour market shares a number of characteristics with other Northern European labour market. Thus there is an unmistakable wage gap between men and women, which can be estimated at between 12 to 19 percent (Deding & Wong, 2004). In the private sector about 10 percentage points cannot be explained by background factors like age and education. In the public sector, the unexplained part of the gender wage gap is almost nil.

Also when it comes to a number of other aspects like choice of education and career patterns, there are still significant gender differences on the Danish labour market (*cf.* Holt *et al.*, 2006).

Figure 5.15: Yearly wages for different skill levels (in 1,000 DKK per year), 2004.



Source: Dansk Arbejdsgiverforening (2004), Table 6.28

## 5.7 LEGITIMACY OF THE UNEMPLOYMENT INSURANCE SYSTEM

As described in section 3, the Danish system of unemployment insurance is based on voluntary membership of private, but state supported funds covering about 80 percent of the wage earners. Since 2001, the Directorate of Labour has conducted yearly surveys to measure the level of satisfaction with the funds among their members. Some of the main results from the latest survey are (Larsen & Ståhle, 2005):

- The members have a positive assessment of the service that they get from their insurance funds; more than 80 percent find that the service is satisfactory or very satisfactory;
- In spite hereof more than a quarter (28 percent) express a low assessment of the usefulness of their membership, even when limiting the sample to those which have experienced unemployment and therefore received unemployment benefits; and
- The members express a high level of solidarity with the fund of which they are members; thus 80 percent see no reasons to consider a shift to another insurance fund.

The low assessment of the usefulness of membership may be related to the compensation rate, which is considerably lower for medium and high-income earners. At least the study shows that the member's evaluation of the unemployment insurance funds is lower, the higher the level of education.

As a supplement to the – generally positive - assessments of the UI-system by the members of the fund described above, one can provide some documentation concerning the general attitudes of the

population towards the level of unemployment benefits and the obligations of the state in this respect. Here one of the repeated observations from studies of the Danish welfare state is the high level of legitimacy of its different elements including the unemployment benefit system (Green-Pedersen et al., 2006: p. 27).

Table 5.3 is taken from a recent study of voters' attitudes towards different elements of public spending and indicates that the voters in general find the level of unemployment benefits to be appropriate in 2001, but also that the balance of opinion has shifted somewhat since the mid-1980s, where voters were in favour of higher benefits. One also notes that the general attitude to the level of social assistance is somewhat less positive.

Table 5.3: Attitudes towards welfare spending, 1979-2005. Percentages and balance of opinion (percentage points).

	2001: the state spends			Balance of opinion: too little minus too much						
	Too little	Appropriate	Too much	1985	1990	1994	1998	2001	2003	2005
Health care	70	27	3	+61	+61	+73	+77	+67	+49	+55
Old age pension	47	52	1	+64	+57	+51	+42	+46	+38	+41
Education	48	50	2	+44	+45	+42	+39	+46	+46	+65
Unemployment benefits (level)	12	75	13	+17	+2	0	-7	-1		
Social assistance (level)	11	65	24	+30	-11	-11	-19	-13		
Aid to developing countries	10	48	42		-26	-35	-10	-32	-12	+5
Immigrants/refugees	12	43	45		-30	-35	-41	-33	-13	-1

Wording: "Now, I'll ask about your view on public expenditures for various purposes. I should like to know whether you think, government spends (1) too much, (2) appropriate, or (3) too little money on these tasks".

Source: Goul Andersen, 2006, Table 4

The same study also gives information about the voter's attitude towards the scope of government with respect to providing a decent standard of living for the unemployed in comparison with some other obligations, summarised in Table 5.4.

When the voters are asked to give priority to unemployment benefits compared to other forms of expenditure, they tend to place them in the second rank, below health care, old age pensions and child care, but still above leisure facilities and reduction of income differences.

Table 5.4: Attitudes towards the scope of government, 2000.

To what extent should it be the responsibility of the government to ...	Definitely	Probably	Probably not	Definitely not	Did not answer	Index 2000 (1-14)
Provide health care for the sick	83	14	2	1	0	1.19
Provide a decent standard of living for the old	71	26	3	0	0	1.33
Provide child care for everybody who needs it	53	35	8	4	0	1.62
Provide a decent standard of living for the unemployed	33	48	16	2	1	1.88
Provide decent housing for those who cannot afford it	39	45	12	3	1	1.78
Integrate immigrants	38	40	13	7	2	1.90
Provide good leisure facilities for children and young people	32	46	18	3	1	1.93
Provide leave arrangements for families with small children	30	46	15	8	1	2.00
Provide leisure facilities for pensioners	28	46	19	6	1	2.03
Provide a job for everyone who wants one	19	44	25	10	2	2.26
Reduce income differences between the rich and the poor	19	27	27	25	2	2.60

Source: Goul Andersen, 2006, Table 5.



## **6 CONCLUDING REMARKS**

Given its long history and development through an ongoing process of political compromises with strong elements of path dependency, it is not surprising that the Danish system of social insurance and labour market policy has developed into a rather complex structure. However, its main traits can be summed up as follows.

Firstly the system still reflects a basic division between those workers that are members of the unemployment insurance funds and those that are not. The first group is under the auspices of a basically state-run system, while the latter are taken care of by the municipalities. With the latest reform to be implemented from 2007 and onwards, the borders between the two systems are weakening (especially with respect to active labour market programmes), but will remain especially, when it comes to the benefit side.

For the insured unemployed the demand for insurances is basically individual in the sense that the choice to become a member of a fund is a choice made by each worker. Given the strong links between the unemployment insurance funds and the trade unions, there is however a strong element of collectiveness in the system due to the fact that the membership of the fund and the union is conceived as a package, although formally being independent of each other. For this reason, the position of the unemployment insurance funds close to the unions is often taken as an explanation of the high degree of unionisation on the Danish labour market.

Also, the financing of the unemployment benefits for the insured unemployed is based mainly on the state (through general taxation), thus giving the benefits the character of a public transfer income, although distributed through private organisations (the unemployment insurance funds). Given that membership contributions are unrelated to risks of becoming unemployed, there are no actuarial elements in the system.

The only example of private demand for and supply of unemployment benefits is the (limited) market for supplementary unemployment insurance that has developed in recent years.

For the non-insured unemployed, which either do not fulfil the membership criteria for the unemployment insurance funds or have chosen not to become members, the (means-tested) benefits are financed through general taxation (central and local) and administered by the municipalities.

The provision of employment services is a public task, although private service providers can enter as sub-contractors for the public agencies (central or local). The state-run public employment service is mainly responsible for the insured unemployed, while the non-insured unemployed are handled by the municipalities. From 2007, a more integrated system will be implemented with the creation of joint job centres combining the Public Employment Service and the social assistance sections of the municipalities. However, as mentioned, the benefit-side will still be based on a two-tier system.

Furthermore, one can emphasise that recent studies and policy discourses has put increasing emphasis on the interplay between the different elements of the system of social security and labour market policy, pointing to the manner in which it is characterised by virtuous circles between an extending safety net provided by social security and active labour market policies on the one hand, and a low level of individual employment protection on the other.

Finally one may consider the issue of winners and losers in the much appraised Danish model of flexicurity (Madsen, 2007). Here, the main groups of winners appear to be large groups of salaried workers, skilled workers and also some unskilled groups. In general, the model provides easier access to a standard employment contract and thus a minor role for temporary workers and agencies.

On the other hand, the main groups of losers on the Danish labour market are indicated by the general growth in the number of adults receiving transfer incomes. This group may not all be in risk of absolute or relative poverty. But they will in many cases suffer from social exclusion due to the important role of working life as a road to social integration in Denmark.

The groups mostly in risk of becoming marginalised are thus immigrants from non-Western countries, some unskilled groups, older workers and persons with health problems. However it is unclear, whether the Danish version of flexicurity in itself is the cause of these exclusionary elements in the Danish employment system. Thus one can argue that a lower level of employment protection has the role of creating winners also among the weaker groups on the labour market due to lower barriers to enter employment. With easier access to dismissing their employees, the employers will also be less reluctant to hire workers, who have had some troubles in their labour market career like long-term unemployment, health problems etc.

Furthermore, within the framework of the Danish model, active labour market policy and policies to support adult education and training has the role of improving the employability for those groups

that are in danger of becoming marginalised. One may see these institutional arrangements also as counterbalancing the risk of firms providing less continued education and training to their employees, due to the risk of losing their human capital investments with employees leaving their jobs.

Looking finally and briefly on the employer's side of the labour market, the main winners in the Danish model will be those firms that experience frequent fluctuations in demand (e.g. within the tourism industry) and the smaller firms, for whom less numerical flexibility could imply higher costs due to the facts that their possibility to apply other forms of flexibility will probably be less than for larger companies.

Taking a longer-term perspective, a number of problems may be identified which could increase the forces that are already causing a rise in the number of persons excluded from the Danish labour market. These include:

- The demographic changes over the coming decades, which imply a growth in the number of older workers, with higher risks of becoming marginalised;
- The rising share of immigrants in the Danish population, with the proportion of persons from non-European countries rising from about 4 per cent today to about 10 per cent in 2020; and
- The increasing wage competition from low-wage countries, also within Europe, which have been amplified due to the entry of a number of Eastern European countries into the European Union.

These challenges to the Danish model will place the need to reduce the upward trend in the numbers of persons left outside the flexicurity triangle high on the Danish political agenda in coming years.

To these challenges one can add the uncertain impacts of the present reforms of the model involving a new structure of governance with respect to labour market policy. Thus, while the major political parties and social partners still support the basic features of the model, a stronger liberal political ideology could gain momentum, which in the longer run might hamper the social balance behind the model.



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## LIST OF ABBREVIATIONS

ADIR	National Directorate of Labour
AMI	National Institute of Occupational Health
AMS	National Labour Market Authority
APW	Average Production Worker
ASK	National Board of Industrial injuries
AT	Working Environment Service
DKK	Danish Krone
DØR	Board of Economic Advisers
EEA	European Economic Area
LO	Danish Confederation of Trade Unions
NAP	National Action Plan for Employment
PES	Public Employment Service
VERP	Voluntary Early Retirement Pay

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June 2000 Caroline van den Brekel en Kea Tijdens
- 00-02 "The toelating van vluchtelingen in Nederland en hun integratie op de arbeidsmarkt."  
Juni 2000 Marloes Mattheijer
- 00-01 "The trade-off between competitiveness and employment in collective bargaining: the national consultation process and four cases of enterprise bargaining in the Netherlands"  
Juni 2000 Marc van der Meer (ed), Adriaan van Liempt, Kea Tijdens, Martijn van Velzen, Jelle Visser.

# AIAS

AIAS is a young interdisciplinary institute, established in 1998, aiming to become the leading expert centre in the Netherlands for research on industrial relations, organisation of work, wage formation and labour market inequalities.

As a network organisation, AIAS brings together high-level expertise at the University of Amsterdam from five disciplines:

- Law
- Economics
- Sociology
- Psychology
- Health and safety studies

AIAS provides both teaching and research. On the teaching side it offers a Masters in Advanced Labour Studies/Human Resources and special courses in co-operation with other organizations such as the National Trade Union Museum and the Netherlands Institute of International Relations 'Clingendael'. The teaching is in Dutch but AIAS is currently developing a MPhil in Organisation and Management Studies and a European Scientific Master programme in Labour Studies in co-operation with sister institutes from other countries.

AIAS has an extensive research program (2000-2004) building on the research performed by its member scholars. Current research themes effectively include:

- The impact of the Euro on wage formation, social policy and industrial relations
- Transitional labour markets and the flexibility and security trade-off in social and labour market regulation
- The prospects and policies of 'overcoming marginalisation' in employment
- The cycles of policy learning and mimicking in labour market reforms in Europe
- Female agency and collective bargaining outcomes
- The projects of the **LoWER** network.



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