

THE EFFECTS OF REFORM SCENARIOS FOR UNEMPLOYMENT BENEFITS AND SOCIAL ASSISTANCE ON WORK INCENTIVES AND POVERTY IN LITHUANIA



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Aim

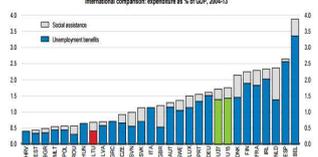
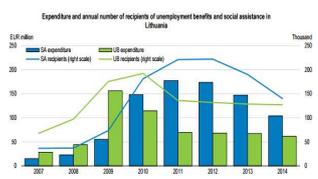
In 2015 the Lithuanian government launched a reform agenda aimed at balancing flexibility of the labour market and of social protection.

We simulate alternative scenarios for reforming the unemployment benefit and cash social assistance in Lithuania.

We look at the effects of reforms on financial incentives to work, poverty, income distribution and their first-order financial costs.

Context

Low protection, low expenditure. Social assistance serves as buffer for joblessness. Trade-off between adequacy and work incentives.[1]



Methods

Reform simulations are carried out using EUROMOD – a static tax-benefit microsimulation model developed for the EU.[2]

Data: 2012 Lithuanian component of the European Union-Survey of Income and Living Conditions (SILC). Reforms modeled as if introduced in 2015.

Simulations reflect intended first-order effects; full benefit take-up and tax compliance assumed.

Indicators of work incentives:

- net replacement rates (NRR),
- participation tax rates (PTR),
- marginal effective tax rates (METR).

Distributional effects and costs:

- First-order impact on disposable income, poverty, GINI and relative change in expenditure.

Unemployment benefit

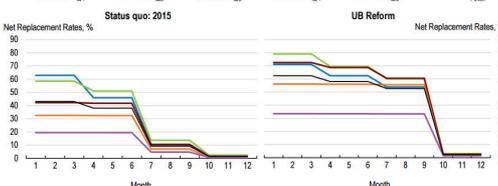
Status quo & Reform

Status quo: weak support in case of job loss; strict eligibility criteria, low duration and a low level of benefits.[3] Reform along the lines planned by the authorities:

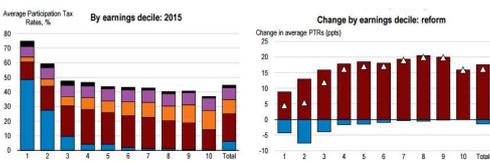
- Increase in benefit amount** to 30% of the minimum monthly wage + 50% of former earnings during the first 3 months (40% between the 4-6 month; 30% between the 7-9 month).
- Increase in benefit ceiling** to 75% of the gross average wage.
- Extended duration** to 9 months + extra 2 months for special groups.
- Reduced required contribution history** to 12 months during the last 24 months.

Results

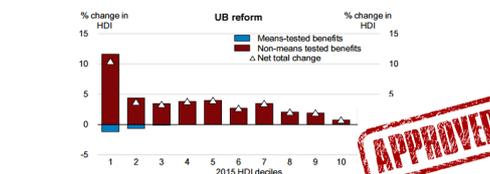
- Increased NRRs across all earnings quintiles from ~22% to ~44%. Those with higher earnings benefit relatively more.



- Increase in PTRs by ~16 ppts on average. Higher effect in the middle and upper part of the income distribution. At the bottom – reform counteracted by withdrawal of means-tested benefits.



- Those at the bottom of the income distribution benefit most from the reform relative to their total disposable income.



Distributional effects and costs

Unemployment benefit reform: increase the number of recipients by ~13% and more than double expenditure (to ~1% of the GDP). Marginal redistributive effect.

Social assistance reforms more profound redistributive effects (except reform A). Increase in the total spending by around 25-65% depending on the parameters of the reform.

Social assistance

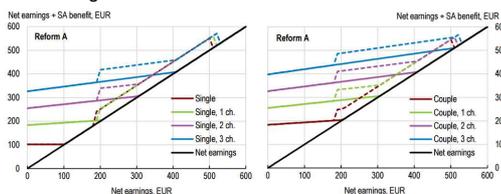
Status quo & Reform

Status-quo: METR at around 90% due to reduction of social assistance with earned income.[1] Low adequacy, especially for singles. Three reforms scenario:

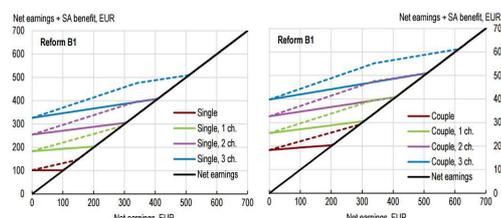
- A. Extension of in-work payments** for assistance recipients unemployed for 6-12 months;
- B1. Introduction of earnings disregard** at 30% (up to 102 EUR);
- C1. Increased state supported income** (130 EUR), **steeper equivalence scale** (original OECD) and **lump-sum supplement for children** (20 EUR).

Results

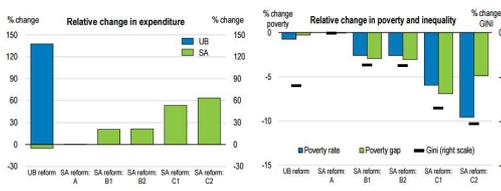
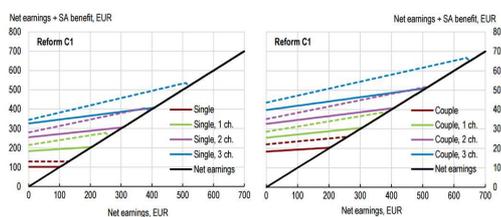
- Limited number of beneficiaries of the reform. Increase in income by ~10-25%. Singles benefit more. Implies a non-linearity in the system. Marginal average decrease of the PTRs.



- Only affects those in work or taking a job. Decrease in METR among the social assistance recipients by ~25 ppts. Working recipients with dependent members (i.e. children) benefit most.



- Affects all benefit recipients. Decrease in METR by 6-13 ppts on average (15-30 ppts for families with children). Helps balance benefit adequacy and work incentives and avoid benefit withdrawal.



This Working Paper is available on the OECD website and relates to the 2016 OECD Economic Survey of Lithuania: www.oecd.org/eeco/surveyoflithuania/

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