

Work incentives/disincentives in Lithuania

Introduction

In Lithuania, the social assistance system is underdeveloped and lacks generosity. State supported income amounts to LTL 350 (EUR 101) per family member, while realistic minimum living standard (MLS) is around LTL 900 (EUR 261). Yet, even such small amounts of money and possibilities to get some compensation of utility charges, along with opportunities to engage in shadow economic activities, encourage certain groups of individuals to evade less-paying official jobs, rather preferring cash social assistance (social benefits) on a long-term basis. In response to such a situation, the Ministry of Social Security and Labour (MSSL) has prepared a number of measures aimed at facilitating employment in social beneficiaries, reducing their social exclusion, increasing community's role (on municipalities' level) and using the funds allocated for social assistance in a more rational way. These measures are desperately needed in the country, which has been demonstrating one of the lowest employment rates in Europe since the beginning of the 21st century. A dramatic growth of unemployment in 2008 led to an increase in the number of social beneficiaries. However, a shortage of those willing to work is more and more often emphasised by employers.

On the other hand, the people's unwillingness to work and their sticking to social benefits are usually determined by low wages and unattractive working conditions offered in the labour market. That is why older people (50+) and lower-skilled individuals get caught the poverty trap, while younger and higher-skilled individuals emigrate or get actively engaged in shadow business activities. This could explain the fact that in a period from 1Q 2010 to 1Q 2011 the total number of the unemployed fell by 16 thousand, while the number of the long-term unemployed grew by 41 thousand and employment increased only by 11 thousand. However, 83 thousand of Lithuanian citizens reported emigration from the country within the same period. Unattractiveness of the Lithuanian labour market and social unsafety can be illustrated by emigration trends in 2011: despite recent economic growth (with annual GDP growth averaging around 6% in Lithuania in 2011), over 50 thousand individuals departed from Lithuania in 2011.

The anticipated measures for improving cash social assistance will be implemented in Lithuania by virtue of the Law Amending the Law on Cash Social Assistance for Low-Income Families (Single Residents) (the Law). Basically, the provisions of the Law are viewed positively, but both scholars and practitioners (employees of municipalities and non-governmental organisations) point out that the statutory provisions are of a punitive nature rather than providing a necessary incentive. The Law does not provide for activating individual work with long-term social beneficiaries and coordination of employment measures for social beneficiaries. Likewise, attention is paid to the fact that reduction of cash social assistance for families with no other income will impoverish them even more and reduce opportunities for social development, especially as regards families with dependent children. Systematic monitoring of the measures implemented must therefore be in place, along with expeditious response, so that the improvement of cash social assistance would not get stuck and the efficiency and social attractiveness of the measures would keep growing.

Below, we discuss the contents of the statutory measures in more detail and provide brief evaluation thereof in terms of work incentives and social implications.

1. Amendments to the Law on Cash Social Assistance

As already mentioned, the amendments to the Law on Cash Social Assistance was adopted by the Parliament of the Republic of Lithuania (PRL) on 1 December 2011. Among other things, the Law provides for a number of measures that are expected to have direct or indirect effects on work incentives/disincentives in Lithuania. The direct measures could include:

1. Supplementary social benefit in case of employment. The Law stipulates that a 50% higher social benefit may be granted to a person who gets employed if he/she: a) got employed for a wage that is not lower than one minimum monthly wage and not higher than two minimum monthly wages (MMW); b) was registered at the local labour exchange (LLE) for a minimum period of 12 months prior to the employment; c) received social benefit at least once during the last three months; and d) has children. This amendment to the Law is expected to ensure motivation of working-age people to get integrated into the labour market, actively look for a job and to reduce long-term dependency on the social assistance system.

2. Gradual reduction of social benefits to persons who receive social benefits for 36 months or more. The Law stipulates that a social benefit shall be reduced to a family (single person), if at least one member of the family receiving social benefit for a period of 36 months or more is a working-age unemployed person: by 20% to families (single persons) receiving social benefit for a period of 36 to 48 months; by 30% to families (single persons) receiving social benefit for a period of 48 to 30 months; c) by 40% to families (single persons) with dependent children receiving social benefit for a period exceeding 60 months; payment of social benefit shall be discontinued to families (single persons) without dependent children receiving social benefits for a period exceeding 60 months. The right to full social benefit shall be acquired again after 12 months' employment during the last 24 months. This amendment to the Law is expected to reduce cases of abuse of social benefits.

The measures with indirect effects on work incentives/disincentives in Lithuania could include:

3. Delegating the granting of cash social assistance to the independent functions of municipalities in pilot municipalities. The Law stipulates that five municipalities shall independently provide social assistance to their residents within a period of three years. If cash social assistance proves to be more efficient in these municipalities (better targeted and fairer assistance provided to those who really need it; effective measures implemented to prevent likely cases of abuse and preserve work incentives; more rational use of fund allocations, etc.), the whole system of granting cash social assistance to the needy in Lithuania would be subject to fundamental restructuring and the granting of social benefits would be delegated to the independent functions of municipalities in all municipalities.

4. Application of the principle of economies of scale in the granting of cash social assistance. The Law sets forth differentiation of the ratios applicable in calculation of social benefits and compensations basing on the number of family members or persons living together: social benefit equalling 100% of state-supported income (SSI) shall be payable to the first person living together, 80% of SSI - to the second one, and 70% of SSI – to the third and the rest of persons living together.

5. Simplifications of conditions qualifying the needy for cash social assistance. The Law stipulates that social benefits, as based on income and property, shall be granted to

persons registered at the LLE irrespective of the length of registration (comparing with a previously applied 6 months' term of registration at the LLE) and to persons registered with a public employment service of a foreign country. This measure is expected to create conditions for receiving cash social assistance when it is needed most (for example, in case of loss of work income).

6. Legalisation of the right to compensation of heating and water costs for lessees.

This measure is expected to create equal conditions for people who don't have their own dwelling and live in a leased dwelling, young families in particular, to receive compensations.

7. Entrenchment of stricter conditions of granting cash social assistance to persons failing to comply with the duties established by the Law.

This provision has mainly to do with the prevention of illegal (undeclared) work and/or illegal (undeclared) income. Detection of the mentioned violations would result in withdrawal of social benefits/compensations from a family/single resident for a certain period of time (6 months).

2. Evaluation of the amendments to the Law

Consideration of the aforementioned measures for the improvement of cash social assistance in Lithuania lasted for some 2 or 3 years. It was already in 2004, when the researchers from the Institute of Labour and Social Research (ILSR) submitted proposals to the MSSL concerning economic measures (supplementary social benefit) promoting employment of long-term social beneficiaries. Therefore, implementation of the adopted measures appears to come (in terms of their relevance) with a delay of 4-5 years. This by itself has negative implications, as a part of long-term recipients of social benefits got used to be passive on the labour market and returning to active employment would be therefore more complicated for them.

Below, we provide expert analysis of each measure and/or its likely effects¹.

1. Supplementary social benefit in case of employment. This measure is to have a direct impact on the motivation of social beneficiaries to take lower-paying jobs, as even

¹ For the purpose of analysis of the effects of specific measures, the authors, due to the lack of experience in the implementation of such measures, have consulted scholars from the Vilnius University and representatives of non-governmental organisations functioning in the area of social assistance.

MMW is currently by some 20% lower than real MLS. Conditions for the implementation of this measure are also viewed as positive. Yet, there are some doubts about the measure:

a) Will social benefits higher by 50% and payable for six month be a sufficient work incentive, if a person is paid only MMW? According to LLE's information, about 35% of registered job vacancies offer MMW. If MMW remains the same or increases insignificantly (by LTL 50-100/EUR 15-30) in future, the measure may lose its attractiveness;

b) Raising of social assistance upon taking a low-paying job distorts market conditions in the area of employment. This may have negative implications for the labour market (balancing labour force by free market mechanisms) and for the relationship between capital and labour, as this reduces employer incentive to increase minimum wages and, at the same time, shift responsibility for low/insufficient income on the State;

c) Application of the measure will require additional resources from the state budget, which debt is already increasing each year. Implementation of the measure does not provide for any mechanism of employers' control to prevent them from offering lower wages to potential employees so that they preserve the right to supplementary social assistance.

To summarise the effectiveness and efficiency of the implementation of the measure, we can say it may lack effectiveness. First, this is because of shifting the problem of low wages to the State (state budget) under conditions when financial abilities of the State are already weak and continue to weaken further. The second reason is the lack of a proper control mechanism and failure to integrate the measure into the system of labour market policies.

In general, the efforts the Government of the Republic of Lithuania (GRL) has finally taken in this area should be welcomed, but these are just the first steps which, due to the above-mentioned reasons, could bring more losses than benefits.

2. Gradual reduction of social benefits to persons who receive social benefits for 36 months or more. It is obvious that the authors of the measure expect it to facilitate social beneficiaries to take paid jobs. However, social benefits in Lithuania are very low and this reduction will weaken household consumption, what is especially bad for families with dependent children. The measure would be more justifiable, if social benefits are by 40-60% higher in Lithuania. According to expert analyses, a share of abusers of cash social assistance

is around 30% of total recipients of social benefits; the rest of them are people who have been caught to the poverty trap due to existing circumstances and their return to the labour market would be difficult without external assistance. Therefore, researchers and some practitioners agree that fines for non-employment could be of little effect, because what is necessary in this regard is more active work with social beneficiaries, facilitation of their motivation, strengthening employability and support for employment. It is admitted that recipients of cash social assistance should be more responsible for their well-being and social benefits should facilitate beneficiaries' activity on the labour market. Yet, we are of the opinion that more attention should be also paid to beneficiary's subjective aspects (disability, place of residence, occupation, etc.).

It might be also reasonable to provide for possibilities and conditions to compensate reduced social benefits in form of in-kind benefits (foodstuffs, etc.) in order to secure minimum consumption of households.

3. Delegating the granting of cash social assistance to the independent functions of municipalities in pilot municipalities. Before adoption of the amendments to the Law, municipalities in Lithuania already enjoyed wide opportunities in exerting influence over the granting of cash social assistance (for example, issue of a statement of investigation into the living conditions, requirement to perform socially beneficial works, etc.). Therefore, some municipalities were quite active and widely used the mentioned opportunities prior to the amendments. On the other hand, there were cases of saving resources for the implementation of social security policy measures by municipalities and using such resources for purposes not meeting their designated use (payment of salaries, payment for construction works, acquisition of motor vehicles, etc.). Therefore, this measure is generally seen as positive because it: increases responsibility of municipalities, creates preconditions for strengthening civic society (raising civic consciousness) and cooperation between municipalities, and for using financial resources in a more rational manner. However, extremely limited financial abilities of municipalities raise some doubts as to their capability to pay more attention to the administration of cash social assistance by developing relationships with NGOs and LLE, to consciousness-raising among social beneficiaries and to the prevention of social assistance abuse by the beneficiaries (articles in local press, meetings at schools, etc.). If the

aforementioned measures are implemented by municipalities from their own resources only, this would presumably affect the beneficiaries' interests.

Likewise, it's worth mentioning that the measure is more useful in small municipalities where community life is more visible.

A positive mention should be made of pilot implementation of the measure, as this is an innovation in the area of social security in Lithuania.

4. Application of the principle of economies of scale in the granting of cash social assistance. Though being viewed positively, this measure will not have great impact on household consumption due to small amounts of money. On the other hand, we believe it is necessary to improve accounting of households, for even small financial disincentives are likely to encourage residents to conceal the fact of living together.

5. Simplifications of conditions qualifying the needy for cash social assistance. This measure is also seen as rather positive and in line with the social beneficiaries' interests, because unemployment and loss of income usually pose more threats to poorer groups of individuals who have fewer opportunities to save for a rainy day. However, we think it could have been reasonable to provide for certain differentiation of the implementation of the measure (i.e., to provide certain waiting periods) subject to disposable income, reasons for losing a job and the number of children in a family. It is out of question that household members need assistance in case of loss of income but, on the other hand, it is necessary to raise consciousness of household members and responsibility for their economic well-being.

6. Legalisation of the right to compensation of heating and water costs for lessees. This measure should be given positive evaluation, too, and might as well be attributed to the measures of direct effect on work incentives. High lease prices for dwelling, high utility charges and low wages greatly limit the internal labour migration. Therefore, the measure is expected to improve attractiveness of leasing a dwelling for low-income families and encourage internal labour mobility which is of particular relevance to young people.

7. Entrenchment of stricter conditions of granting cash social assistance to persons failing to comply with the duties established by the Law. This measure triggered the most expensive debate about it. It is admitted that various efforts should be taken to encourage incentives to refrain from shadow economic activities and to restrict opportunities to abuse

cash social assistance and compensations. However, the measure appears to have many bottlenecks. First, attention should be paid to the loose definition of the procedure for detecting illegal employment and/or illegal income. It is necessary to provide for clear principles of relating the decision to discontinue social benefits to information possessed by the State Labour Inspectorate or the State Tax Inspectorate, or to institutionalise this provision otherwise. Second, it is not clear how minimum household consumption will be ensured after withdrawal of social benefit in cases when income from 'shadow' economic activities is only of an accidental nature? Third, implementation of this measure requires more active abuse prevention, such as better-targeted and wider dissemination of information to beneficiaries, preparation of leaflets containing relevant information, dissemination of information to employers and NGOs, organisation of public debate. We believe it is far more important to discourage people from abusing social assistance rather than to punish them. Therefore, primary focus should be placed on the development of preventive measures in this regard.

On the other hand, we should not omit the fact that, under conditions of generally very low level of cash social assistance in Lithuania, engagement of social beneficiaries in shadow economic activities often allows these people to survive and ensure, at least to a certain extent, sufficient subsistence conditions. Therefore, strict weaning of social beneficiaries away from the participation in shadow economic activities will considerably affect their living standards and push them into deeper poverty and social exclusion. This may have extremely negative implications for families with dependent children.

3. Other disincentives to work

The first and the main reason of insufficient motivation to work among Lithuanian residents is low wage level. Particular attention should be paid to MMW (LTL 670 net), which is by some 20% lower than real MSL.

Another reason is low transparency in determining remuneration for work. Many people (particularly, in the private sector) are not aware of the grounds for being paid a certain wage and conditions of changing the amount of wage. Frequent abuse of such a dominant position by employers leads to extremely high differentiation of living standards in Lithuania.

Special emphasis should be given to high salaries in Western Europe, as compared to Lithuania. It's not that Lithuanian people do not want to work at all; it's about unwillingness to take low-paying jobs in Lithuania. Instead, people are more willing to take various jobs in emigration which, though often unattractive in terms of working conditions, ensure considerably better balance between income and basic expenses.

One more reason of unwillingness to work in Lithuania is uncertainty of career opportunities. Personal contacts and family connections play an important role in accessing employment both in the public and private sectors in Lithuania. This undermines the professionalism and competencies of educated youth and more skilful employees.

Disabled individuals account for a significant portion of the working-age unemployed. Organisation of social assistance to such individuals is quite passive and not encouraging to look for a job more actively. As a result, as few as some 10-15% of disabled people are employed in Lithuania.