

Work incentive and other effects of social assistance and unemployment benefit policy in the Czech Republic*

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Abstract. In this paper we provide an account of most of the passive labor market policies (unemployment compensation, social assistance, state social support and the pension system) in the Czech Republic during the 1990–1996 period. The eligibility requirements and benefit levels are described in great detail. Using Labor Force Survey data, we compare the characteristics of unemployed people receiving unemployment benefits with those receiving social assistance and those not receiving any benefits and we find significant differences in their characteristics. Finally, we provide an analysis of the work disincentive effects of the unemployment and social assistance benefits by comparing these benefits to market wages and by analyzing the effect of being in the system on the duration of unemployment of two cohorts of unemployed in 1994 and 1995. We find that social assistance benefits are fairly generous for low income families with more children, individuals with these characteristics have a higher probability of receiving social assistance and they tend to stay unemployed longer than those people with relatively fewer dependants. We conclude that the social assistance scheme seems to be having some disincentive effects for at least one group in the population.

Key words: Czech Republic, passive labor market policies, unemployment duration

JEL classification: H53, I38, J64, J65, J68

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Introduction

This study contributes to our understanding of the work incentive effects of the income maintenance schemes for the unemployed in the Czech Republic. It begins by updating the description of structure of social assistance and unemployment compensation presented in Terrell and Munich (1996) and proceeds with an analysis of the characteristics and labour supply behaviour of the persons taking part in these schemes. We would like to know to what extent people on these income maintenance schemes differ from other unemployed people and whether or not people in these schemes are more likely to stay unemployed longer than those who are not taking part in these schemes.

More specifically, we begin in Part I by briefly reviewing the structure of the various income maintenance schemes, namely unemployment benefits, social assistance, social support and pensions, with special emphasis on the changes introduced at the beginning of 1996 (Sections 1 and 2). We then take a look at the relative magnitudes of the benefits and their potential incentive effects in Section 3. In Section 4, we describe how the systems are financed.

In Part II we proceed to analyse the characteristics of the people receiving unemployment benefits and social assistance. We begin in Section 5 by discerning the magnitude of the population receiving income support of each type and the extent to which individuals rely on both schemes vs. just one. We then compare the characteristics of unemployed people supported by these two systems and ask to what extent do they differ. We rely on the results from our analysis of *Labour Force Survey* (LFS) quarterly data over the 1994–1995 period as well as the results of one other study based on a smaller more specific survey. In Section 6, we assess the relative impact that these two programs have on the probability of leaving unemployment by estimating hazard functions with LFS data on two cohorts of unemployed individuals in two years (1994 and 1995). We draw conclusions and delineate the resulting unanswered questions in Part III.

Part I: Passive benefit systems 1990–1996

1. The unemployment compensation system¹

An unemployment compensation system (UCS) was put into effect January 1, 1990 and it has undergone several changes since. It began as a generous one until reforms put into place on January 1, 1992 made the level of benefits (based on wage replacement rates) and eligibility criteria more restrictive. In January 1996, new reforms increased the replacement rates for the new entrants and certain other groups of unemployed and broadened again the eligibility criteria.

Eligibility: Only a job seeker registered at the district Labour Office qualifies for unemployment benefits.² In 1990–1991 basically the only additional con-

¹ This section is only a brief description based on a more detailed analysis in Terrell and Munich, 1996.

² A person can qualify for unemployment and social assistance benefits only if registered, available for work and co-operating with the office in job search activities. Those who are not imme-

dition was a minimum of twelve months work within the previous three years. This work period could be substituted with a number of different situations (such as care for own child until the age of three, imprisonment, registered unemployment, full time study and others). From January 1, 1992 to January 1, 1996, the period of employment could only be substituted with a period of study. In 1996, however, the former broader eligibility criteria have been put back into effect. The administrative records from the Ministry of Labour and Social Affairs suggest, however, no increase in the share of the unemployed receiving unemployment benefits as one would expect after broadening of the eligibility rules. By the end of the second quarter of 1995 this share was 43.4% and by the end of 1995 it had risen to 44.2%. However, by mid-1996 it reached 44.4%, i.e. it has not changed significantly.

Entitlement: Prior to January 1, 1992, the unemployed were entitled to receive benefits for twelve months, since then, the entitlement period has been six months. Periods of sickness, maternity leave or participation in government-subsidised job placement programs (during which benefits are replaced by other sources of income) are not deducted from the entitlement period.

Benefits: In 1990–1991, the replacement rate varied depending on the reason for layoff (e.g., up to 90% for the first six months for those laid off for organisational reasons). From 1992 to the present, the replacement rates are unified on 60% of the previous net wage for the first three months and 50% for the next three months. Since 1990, those in training programs have received 70% of their previous net average wage while participating in the program. From 1992 to 1995, the maximum level of benefits was set at 1.5 times the minimum wage (1.8 times for those in retraining). In January 1, 1996 the base for the maximum changed to the minimum living standard for an adult in a one person household.³ There is no minimum benefit since 1992. Benefits are not indexed to inflation, nor are they taxed.

Until the end of 1995 the wage base for the unemployment benefit received by labour force entrants was the minimum wage. As of January 1, 1996 the base has been changed to the minimum living standard for an adult in a one person household (2,660 CZK at that time, 2,890 CZK currently). This change has raised the benefit in the first three months of unemployment from 1,320 CZK in 1995 to 1,596 CZK in January 1996 and further to 1,734 CZK since October 1996.

2. Social assistance system⁴

Unlike the unemployment benefits, the social assistance system was established before 1990. However, several legal changes and new components were

diately available for work can also register at the district Labour Office, but in a different category and do not qualify for unemployment benefits. Persons who are struck from the register for non-co-operation cannot be re-registered for three months.

³ The minimum living standards will be described below.

⁴ In order to limit the scope of the paper, we have left out certain parts of the social assistance systems, such as sickness benefits (except maternity-related), the sphere of social institutions for the aged and disabled and old-age and invalidity pensions as these have many specific features and aims.

introduced in 1991–1994, and a new and substantially revised social assistance system was partially passed by the Parliament in 1995. Parts of it (e.g., parental benefits) came into effect in October 1995 while other parts (e.g., child allowances) came into effect in January, 1996. Reform of the remaining old schemes is still being drafted and is expected to be presented to the Parliament in 1997.

The new social assistance system aims to cover a wide range of causes of social necessity. It is composed of three major norms: the first – *Social Assistance* – supports those who are in a financial or social need and are unable to raise the income themselves or with the assistance of their family; the second – *State Social Support* – provides benefits for families raising children; and the third – *Social Insurance* – provides social security through a pension system, sickness and employment-injury benefits.

2.1 Social assistance

Law no. 23/1991 establishes the right for everyone who is in material need to “assistance as is essential for ensuring the basic living conditions with the proviso set by law.” Following this, Law no. 463/1991 established the *minimum living standards* (MLS). Anyone whose income is determined to fall below the MLS is eligible for social assistance benefits equal to the difference between their income (in the last six months) and the level of the MLS. (See the appendix for a more precise definition of how the household income is calculated.) A household has to re-apply for social assistance (SA) benefits every six months and in principle is entitled to these benefits as long as its income falls short of the MLS. Any unemployed member of the household must be registered at the district labour office in order for the household to be eligible for SA benefits.

The MLS is uniform across the country despite the presence of significant regional differences in the cost of living. Since the cost of living is, in general, lower in high unemployment regions, the uniform social assistance benefits might thus discourage job search in particular in these low-cost districts.⁵

The levels of MLS for different categories of individuals and households are presented in Table 1. For each person his/her MLS is computed as a sum of two parts: i) the personal minimum, which is a function of age; and ii) the household minimum, which is a function of the number of individuals living together as a household. MLS for individuals with particular needs (e.g. The health problems) is further increased by 600 CZK per month.

The MLS levels are indexed on a regular basis. Until 1995 they were changed whenever inflation (measured by the CPI) had risen by more than 10% since the previous indexation. Since January 1995, the threshold of inflation was decreased to 5% reflecting the fall of the aggregate inflation level in the country. According to the law, the extent of indexation should “take into the account the extent of the cost-of-living increase,” but no exact guidance is provided. The size of the increase is thus fully at the discretion of the government. Up to now, the rate of increase of the MLS has been equal to the changes in the CPI index.

⁵ See Erbenova (1995) for some empirical evidence on the regional disparities in wages and unemployment rates.

Table 1. Individual and household minimum living standards (nominal, monthly CZK)

	1992	1993	1994	1995	1996 January–Sept	1996 from Oct. 1
Individual minimum						
<6 years	900	1020	1120	1230	1320	1410
6–9 years	1000	1130	1240	1360	1460	1560
10–14 years	1200	1360	1500	1620	1730	1850
15–26 years	1300	1470	1620	1780	1900	2030
>26 years	1200	1360	1500	1680	1800	1920
Household minimum						
1 member	500	600	660	760	860	970
2 members	650	780	860	1000	1130	1270
3–4 members	800	960	1060	1240	1400	1570
>4 members	950	1140	1260	1400	1580	1770

Note: Both the individual and the household minimum are changed by the government decree whenever the consumer inflation exceeded a pre-specified level since the last increase. See the text for more details.

2.2 State social support

The goal of the new social support system,⁶ which came fully into effect in January 1996, is to make the benefit structure more consistent with the operation of the market economy. The main objectives pursued by the government in reforming the scheme can be summarised as follows:

- change in the mechanism of benefit disbursement
- greater emphasis on means-tested schemes
- targeting of benefits primarily towards poorer families
- clarification and simplification of the eligibility criteria and application process
- unification of all types of the benefits paid to families with children under one legal norm, reduction in the number of different benefits and rationalisation of their structure
- introduction of allowances in response to new social problems (e.g., benefits covering travel expenses and housing expenses)

The need to change the system of benefit disbursement followed from the transformation-related increase in the number of employers. Under the previous system, all these benefits were physically disbursed by the employers.

⁶ Laws no. 117/1995 and 118/1995 and their amendments.

As the number of employers grew from about 8,000 in 1990 to more than 33,000 in 1995, the control and administration of this system became unmanageable. Furthermore, unemployed, self-employed and employees of small enterprises received their benefits at the district level offices of the Social Assistance Administration. Hence, there were two distinct ways of disbursing and administering the system implying further control problems. It was decided that all the eligibility decisions and disbursement of the benefits would be administered by the state at the district level.

Prior to the current system, families were entitled to the whole package of family benefits, irrespective of their income. The original draft of the new social support system proposed that all the family benefits would be means-tested (with the exception of foster-parent care benefits). However, the resulting law passed by Parliament contains both means-tested and non-tested benefits. Minimum living standards serve as a basis for the determination of both the eligibility for and amount of the family allowance. This way, both the levels of the benefits and the eligibility criteria are automatically indexed whenever MLS's are changed.

Social support benefits are paid to all persons residing on the territory of the Czech Republic. This means that the permanent residence of a person and not his/her nationality is decisive. Hence, foreigners with a long term legal residence status are also eligible.

We now turn to the description of major benefits comprising this system.

2.2.1 Means-tested family benefits:⁷

i) *child allowances* – supplementary income for the purpose of raising a child. *Level of benefit:* From January 1993 to October 1995, the amount of the monthly allowance was only a function of the age of the child, ranging from 340 CZK (for a child less than six years of age) to 490 CZK (for a child over 15 years of age).⁸ Since October 1995, the size of the benefit depends also on the household income. *Eligibility:* Families with income of up to triple the MLS for their type of family are eligible for some allowance. If the total income is less than $1.10 \cdot \text{MLS}$ for their family type, the benefit equals $0.32 \cdot \text{MLS}$ of a child for each dependent child. Families with income in the range of $1.10 - 1.80 \cdot \text{MLS}$ are eligible for $0.28 \cdot \text{MLS}$ of a child for each dependent child. Families with income in the range $1.80 - 3.00 \cdot \text{MLS}$ are eligible for $0.14 \cdot \text{MLS}$ of a child for each dependent child. *Entitlement* lasts as long as the child is dependent. A parent has to re-apply each year and the family income during the preceding year is tested. A *dependent child* is defined as any unmarried child under the age of 26 years as long as he/she is a student in a defined type of secondary or higher educational institution or cannot (due to a long-term sickness or disability) earn any income. A person under the age of 18 who is registered as unemployed and not receiving unemployment benefits is considered to be a dependent child. (A married person can be a dependent child only if that person is married to another dependent child.)

A family with two children (6 and 12 years of age) and with a net average

⁷ See below for the definition of income for the purpose of means testing.

⁸ Before 1993 the allowance was a function of the total number of children in the family, where the marginal increment was positive.

monthly income in 1994 of 10,647 CZK (= 1.3*MLS in January 1996) was eligible for a child allowance of 409 CZK for the younger and 484 CZK for the older child. These allowances thus comprised an addition of about 8.4% to the net income of this family. The share rises dramatically for the lower income households. A household earning 75% of its MLS (6,143 CZK) qualified at the same period for a total allowance of 1,021 CZK or some 17% of its net income. Such a family would also qualify for social assistance since its income, even after adding the children allowance, was still below the MLS for that family. The additional SA benefit would be 1,027 CZK.

ii) *social allowance when caring for a child* – additional supplementary income for raising a child. *Eligibility*: a family with at least one dependent child and having an income below 1.6*MLS. *Entitlement*: the length time the family's income is below 1.6*MLS and the child is still a dependent. A parent has to re-apply quarterly. The income of the preceding *quarter* is tested. The *level of the benefit* is defined as follows:

$$SA = MLS1 - \frac{MLS1 * I}{MLS2 * 1.6}$$

where: *SA* = social allowance when caring for a child

MLS1 = sum of individual minimum living standards of all dependent children

MLS2 = minimum living standard of the family (sum of individual standards and household minimum)

I = family income

The benefit is scaled up further when either the children or the parents are sick with a long-term illness or disabled, or when the household is formed by a single parent (the scaling coefficients are different for each situation). Hence, the family in the previous example for child allowances would be eligible for an additional 559 CZK per month for the duration of one quarter. If the older child in this family were sick with a long-term illness, the family would instead be eligible for 730 CZK per month.

iii) *benefit to cover housing expenses* – *Eligibility*: A household is eligible when the joint income of all persons permanently residing in a flat falls below 1.4*MLS for this type of a household, irrespective of the ownership type of the flat (also inhabitants of the self-owned flats are eligible) and irrespective of the actual housing expenses. A household has to re-apply quarterly and the income of the preceding *quarter* is tested. The *level of the benefit* for the house defined as follows:

$$HB = MLSh - \frac{MLSh * I}{MLS * 1.4}$$

where: *HB* = housing benefit

MLSh = household minimum (part of the minimum living standard related to the household expenditures)

MLS = minimum living standard for the household (sum of individual standards and household minimum)

I = household joint income

(iv) *benefit to cover transportation expenses* – is a benefit introduced after the subsidies to pupil and student transport fares were phased out. Any dependent child studying in a municipality different from his/her permanent residence municipality is eligible. Families, where children did not complete compulsory schooling (9 years), are eligible for the benefit irrespective of the family income. If a dependent child studies at the secondary or higher educational institution, only a family with income below 2.0*MLS is eligible. Construction of the benefit level is very detailed and the resulting sum depends on the type of a school attended and regularity of transportation (daily, weekly, etc.). Entitlement is established yearly.

2.2.2 Non-tested family benefits:

i) *parental allowance* – a payment to a parent caring personally full-time for a child under the age of four or a handicapped child under the age of seven.⁹ I.e., the child must not be placed in nursery, kindergarten or any other institution for pre-school children. A parent is eligible for the benefit if he/she does not earn any income and does not receive health insurance or maternity leave benefits. The only exceptions are when the net income earned by the parent is less than or equal to his/her personal MLS or if the employment contract implies no more than two hours of work per day. In 1994 the maximum benefit was defined as a lump sum and represented 79% of the minimum wage. Currently, the size of the benefit is defined as 1.1 times the personal MLS of the parent. As of October 1996 the benefit was 2,112 CZK or 84% of the minimum wage.

ii) *benefit at the birth of a child* – is a one-time benefit provided upon the birth of a child. The size of the benefit is a multiple of the individual MLS of a newly born child (currently 1,410 CZK) and depends on the number of children born simultaneously, rising nonlinearly.¹⁰

iii) *foster care benefits and benefits for families of conscripts* – Foster care benefits include allowance covering the individual nutrition needs of a child, remuneration for the foster parent, one-time start-up allowance (equivalent to the benefit at birth), allowance for buying a motor vehicle (70% of the price with a maximum limit when caring for at least 4 children). Children of military conscripts and their spouses caring for a child below the age of four are eligible for the benefit of 0.67*MLS for their respective individual needs.

iv) *lump sum funeral benefit* – is paid to a person that organised a funeral and is fixed at 3,000 CZK.

All of the social support benefits are non-taxable but are included in the income of a household applying for the income support under the system of Social Assistance.

2.3 Social insurance

An exhaustive analysis of the Czech social insurance system is obviously beyond the scope of this paper. Hence, in this section we briefly review the recent

⁹ Before 1995:3, the child had to be less than three years old.

¹⁰ The benefit for the birth of a child is 4.0*MLS when one child is born, 5.0*MLS per child when two children are born and 9.0*MLS per child when three or more children are born.

changes in the system of old-age pensions and maternity-related benefits, in so far as they influence the functioning of the labour market.

2.3.1 *Support in maternity*

Maternity benefits – women can receive 28 weeks of maternity leave (37 weeks for single mothers) with a benefit equal to 69% of their gross daily wage for the full calendar month (30–31 days). The upper ceiling for the daily wage is set at 270 CZK, thus the implied monthly ceiling is at 8,100–8,370 CZK (for 30 and 31 days, respectively). A woman can therefore receive as much as 5,589–5,775 CZK in benefits which are non-taxable. This is more than 2.5 times the minimum wage or 78% of the average wage in 1995.

Income equalising benefit during pregnancy and maternity – is paid to a either pregnant woman or a woman who has delivered a child within the last nine months who cannot for the reason of pregnancy or maternity perform her original work and is transferred to a different post with lower wage. The benefit is equal to the difference between the original wage before her transfer to a different post and her wage after the transfer, with the maximum for the pre-transfer wage set at 270 CZK daily.

2.3.2 *Pension system and early retirement arrangements*

The current pension system is financed on a pay-as-you-go basis and faces problems of population ageing similar to those in all developed countries with pay-as-you-go pension schemes. The government has so far addressed these problems by reforming the pay-as-you-go system and by introducing the possibility of private pension co-insurance. In January 1996 the new Pension Insurance Bill which came into effect changed the retirement age, the conditions of early retirement and the calculation of the pensions.

Pension benefit: Under this new system, the old-age pension consists of two parts which are both regularly indexed:

- a fixed lump sum to which every pensioner is eligible (920 CZK, and as of October 1996, 1,060 CZK per month);
- a portion related to the pensioner's previous contributions. Simplifying, one can say that this portion is equal to 1.5% of the average gross monthly salary (currently averaged over the last ten years of work and scaled up according to the recent wage inflation) times the number of years that the pensioner paid insurance.¹¹

During the next ten years the pension for a newly retired will be calculated according to both the new and the old rules, the retiree will receive which ever is higher. Pensions are not taxed.

¹¹ The resulting base average monthly salary is also progressively reduced according to a certain algorithm by which only a proportion of the salary less than 1 is taken into consideration in higher income brackets.

If a person wishes to continue working beyond the retirement age without collecting his/her pension, the pension rises by 4% for each year worked beyond the retirement age. When a pension is collected simultaneously with earnings from a secondary activity, the income earned in these activities cannot exceed two times the MLS during the first two years of retirement. The penalty is withdrawal of pension benefits. After the two years, there is no limit on the income earned simultaneously with collecting a pension.

The average (net) pension in 1996 was equal to about 44% of the average gross wage and about 56% of the average net wage, while in 1989 the respective numbers were 50% and 64%. As with the MLS levels, both parts of the pension are regularly indexed whenever the consumer price index has risen by 5% since the last indexation. In practice, pension indexation exceeds consumer price inflation but is lower than the nominal wage growth. (Until now, about 2/3 of the gap between the two has been closed by the indexation). Gradually, the indexation is envisaged to increase the relative importance of the lump-sum portion at the expense of the contribution-related portion. The state financed pension system is thus expected to play more and more a solidarity role, while the insurance (income replacement) function will be left to private co-insurance.¹²

Retirement age: The new Pension Bill is raising the age of retirement incrementally until the year 2007. For men, the retirement age of 60 years (in 1995) is being raised by two months every year. For women the retirement age in 1995 was between 53 and 57, depending on the number of children raised. These ages are being increased every year by four months. Hence, in 2007 the retirement age should reach 62 years for men and 57–61 years for women.

Early retirement: Rather generous regulations concerning early retirement were introduced in 1988 and were tightened only at the beginning of 1993. The 1988 regulations did not impose minimum unemployment criteria for early retirement, nor did they prevent pensioners from combining pensions with earnings from secondary activities. The regulations were changed in 1993 and then again in March 1994. Under the new comprehensive law, people who retire early can not work and draw a pension simultaneously. A person has to be registered as unemployed in the district Labour Office for at least 180 days before he/she can retire early. For those who retire less than two years before their legal retirement age, the pension benefit is lowered by 1% of the base for each 920 day period remaining between the age of retirement and the official retirement age. The pension benefit is then recalculated according to the general rules when the person reaches the official retirement age. For those who retire voluntarily two to three years prior to the official retirement age, the 'regular' pension is lowered by 0.6% for each 90 days and its level is not changed once the retirement age is reached. No pensions are given to those who voluntarily retire more than three years prior to their retirement age.¹³

¹² There are currently some 40 private pension funds in the Czech Republic with the total of 1.3 million people insured (about 25% of the labour force).

¹³ An amendment to the Pension Insurance Bill that further relaxes conditions for the early retirement has been recently passed by the Parliament.

3. Relative magnitudes of the benefits and their incentive effects

The incentive effects of the passive labour market policies on labour market decisions can be inferred by comparing their magnitudes to the mean wage or the minimum wage.¹⁴ As the numbers in Table 2 indicate, the MLS is relatively high compared to the unemployment benefit. In 1992 a person living alone could receive 1,700 CZK as social assistance or if unemployed would on average receive 1,450 CZK as an unemployment benefit. The social assistance for large families appear to be higher – a family of four could receive benefits equal to between 103% and 118% of the average gross wage in the economy and not work. For low income workers this might be an attractive option.

The pitfall of any such comparisons, however, lies in the fact that no benefits are taxed. The tax code in the Czech Republic is relatively complicated and it is not possible to infer the average net wage from the gross wage data published by the Czech Statistical Office. A number of tax deduction allowances (e.g. children, spouse, transportation expenses, etc.) complicates these estimates. Usually, it is assumed that the net wage represents on average about 78% of the gross wage.¹⁵ When this rule of thumb is applied to the data in Table 2, the MLS for the four member household in 1992 becomes 151% of the average net wage.

An important point drawn for the statistics in Table 2 is that both the unemployment benefit and social assistance benefit have fallen as a proportion of the average wage since 1991. The maximum unemployment benefit fell from 92.4% of the average gross wage in 1991 to 40.4% of the average wage in 1995 and has risen slightly in the first half on 1996 to 43.8%. The average unemployment benefit has also declined substantially but most of it came in 1992. Average benefits were 49.3% of the economy-wide average wage in 1991, 31.6% in 1992 and bottomed out at 25.2% in 1995. As with the maximum benefits, the average level rose in the first half of 1996 to 32.9% of the economy-wide average wage. The MLS has also declined, but not to the extent that unemployment benefits have. Their decline has been however more steady. The MLS for an individual living alone declined from 37% of the average wage in 1992 to 29% in the first half of 1996. The MLS for a family of two adults and two children began at 118% of the average wage in 1992 and was 90% of the average in the first half of 1996. Hence the overall conclusion from the table is that in general passive benefits have eroded vis a vis the market wage. Moreover, the value of the unemployment benefits has fallen relatively more than the MLS.

In Table 3 we present data on social support benefits post-reform, in June 1996. The data indicate that the relatively high level of income defining eligibility for the social support benefits (e.g., in the case of the child allowances up

¹⁴ In addition to the minimum wage (which is largely an accounting coefficient for calculating the state contributions to the health care and other funds for the unemployed, children and pensioners), the employment legislation defines the so-called *minimum tariffs*. These are dependent on the tenure of a worker, his education and a type of job and are applied in the firms with no collective agreement between the trade union and employer on wages. No employee can earn a wage lower than the minimum tariff. Depending on the level of education the minimum tariffs for persons with no experience currently range between 2,340 and 5,350 CZK. Hence the current minimum wage of 2,500 CZK is low in comparison to the minimum tariff.

¹⁵ See for instance Bastyr et al., 1995.

Table 2. Types of compensation in the Czech Republic (average, nominal CZK/month)

Type of Compensation	1991	Index %	1992	Index %	1993	Index %	1994	Index %	1995	Index %	1996 2Q ⁶	Index %
Inflation Rate (CPI, yearly)	56.7%	-	11.1%	-	20.8%	-	10.2%	-	9.1%	-	8.7%	-
Economy-wide Wage ¹ (CZK)	3,247	100.0	4,590	100.0	5,459	100.0	6,618	100.0	8,171	100.0	9,119	100.0
Minimum Wage (CZK)	2,000	61.6	2,200	47.9	2,200	40.3	2,200	33.2	2,200	26.9	2,500	27.4
Unemployment Benefit (CZK)												
Mean	1,601	49.3	1,450	31.6	1,585	29.0	1,895	28.6	2,056	25.2	2,996	32.9
Maximum ²	3,000	92.4	3,000	65.4	3,300	60.5	3,300	49.9	3,300	40.4	3,990	43.8
Minimum Living Standard (CZK) for a:												
One adult member household ³	n.a.	n.a.	1,700	37.0	1,960	35.9	2,160	32.6	2,440	29.9	2,660	29.2
Two member household ^{3,4}	-	-	3,050	66.4	3,500	64.1	3,860	58.3	4,360	53.4	4,730	51.9
Four member household ^{3,6}	-	-	5,400	117.6	6,170	113.0	6,800	102.8	7,580	92.8	8,190	89.8

Source: MoL and Statistical Office of the Czech Republic.

Notes:

¹ Average gross monthly wage. Excludes small firms with less than 25 employees.

² Starting from 1996 the maximum is related to the minimum living standard and equals 1.5*MLS for all registered unemployed and 1.8*MLS for those retraining. Until then the maximum was defined as a multiple of the minimum wage.

³ Sum of the two parts, see the explanation in the text.

⁴ Two adults

⁵ Two adults with two children, one 6 years old, and one 10-14 years old.

⁶ Since October 1, 1996 the minimum living standards, and thus the maximum unemployment benefit and other benefits have changed (see Table 1). After this change the MLS for our three types of households was respectively: 2,890; 5,110 and 8,820 CZK.

As the benefits are not taxed it would be better to compare the minimum living standards to the *net* wage. The Czech Statistical Office unfortunately publishes only the gross wage statistics. Estimation of the net wage is not straightforward due to the relatively complicated tax system. Nevertheless, some estimates are presented in the text.

Table 3. Expenditures on and the number of recipients of the social support benefits in June 1996¹

Type of benefit	Total number of recipients (thousands) ³	Total expenditures (mil. CZK) ⁴	Share of total expenditures (%)	Average benefit (CZK monthly)
Child allowance	2230	1080	42.6	455
Social allowance	561	598	23.6	881
Housing benefit	198	69	2.7	280
Travel cost benefit	331	97	3.8	236
Parental allowance	309	615	24.3	1951
Allowance for families of conscripts	3	3	0.1	n.a.
Foster care allowances ²	8	12	0.5	n.a.
Benefit at birth	5	38	1.5	n.a.
Funeral benefit	5	23	0.9	3000
Total	3648	2534	100.0	–

Source: Ministry of Labour and Social Affairs.

Notes:

¹ Data presented for a particular month rather than for the entire year because a household can be recipient of the benefit only for some part of the year due to the means testing.

² Foster care allowances represent the aggregate of four different benefits paid to foster parents.

³ Number of recipients represents households that were eligible since May 1996 and whose eligibility was established in June 1996.

⁴ Total expenditures are actual expenditures on benefits in June, i.e. including the expenditures on benefits paid retrospectively to those whose eligibility in previous months was established only in June. For this reason we cannot use the data in the table to establish accurately the average benefit where it was not available.

to triple the MLS of the family) results in a large number of benefit recipients: 3.6 million in June 1996 or one-third of the population. Hence, the original aim of targeting benefits primarily towards poorer families has thus been compromised. The most widely received benefit (over 2.2 million recipients) is the child allowance. Approximately 86% of all the dependent children in the country received a child allowance in June 1996, of which 47% were eligible for the highest level of allowance, 41% were eligible for the middle level and 12% for the lowest one. Moreover, one-third of the families with children (about 561,000) qualified for the supplementary social allowance. The number of children eligible for this allowance clearly varies during the year whenever the MLS's are changed. According to the estimates of the Ministry of Labour the share of eligible children receiving these benefits should vary within 70–86% of all children.

Despite a stable downward trend in the number of newly born children

since the start of the transition, the number of parents collecting a parental allowance rose as a result of the prolonged entitlement to this benefit when the cut-off age of the eligible child was raised from 3 to 4 years. While in January 1996 some 295,000 parents qualified for this benefit, the number rose to 309,000 by June 1996. This nearly 5% increase can be attributed solely to the prolonged entitlement. The average benefit (which is untaxed) represented 21.4% of the economy-wide average gross monthly wage. The data since the beginning of transition suggest that women fall into unemployment disproportionately and tend to stay unemployed longer than men. The problem might be further exacerbated by this incentive for longer career breaks, which is likely to be used predominantly by lower-income less-educated women.

Despite the above-mentioned qualifications, the 1996 reform of the social support system was nevertheless a step in the right direction, as it attempted to target benefits towards the needy. In 1995, when the reform of the social support scheme commenced, the non-tested benefits represented some 76% of the total spending on social support. By mid-1996 this share had fallen to 30%. The share of social transfers in the total household income changed over time, depending on the overall family income. While the share of social transfers to average income households with children fell during the last 2 years by 2.4 percentage points, this share rose by 5.3 percentage points for the low-income households with children. For these low-income households social incomes (defined to include social assistance, social support, pensions and sickness benefits) represent about 40.8% of their total income in 1996.

Incentive problems related to the UB and SA systems are, however, further exacerbated by the fact that the SA benefits do not readily distinguish between those who work and receive an income insufficient to finance basic needs and those who depend on the state without working. The transition from one system to another often does not entail any loss of income. As our simulations presented in Tables 4–6 show, the effect of exhausting the UB eligibility is felt only in certain types of households. In the single adult person family type this transition affects replacement rate only in the highest income brackets (for those initially earning wages above the economy-wide average)¹⁶ Movement from the UB to the SA benefits does not affect families with only one working spouse under a wide range of assumptions about his income. These families experience a sizeable drop in income already when this spouse becomes unemployed due to the existence of the upper ceiling on UB and they immediately qualify for the SA benefits from the very start of the unemployment spell. Only for the two-earner families with children the replacement rate falls significantly after the UB eligibility has been exhausted. Overall, the job search incentives are thus present primarily after the transition from employment to unemployment when a significant income loss is experienced. Replacement rates are highest for low income families with one working spouse and for the low-income single adult households. As the unemployed from low-income families are subject to greater risk of long-term unemployment, and as in the typical Czech household both adults are working if children are above the age of 3–4,¹⁷ this low UB/SA transition effect may further inhibit job search incentives.

¹⁶ Note that about 60% of employed earn currently wages below the economy-wide average.

¹⁷ Until then a non-working parent qualifies for the parental benefit.

Table 4. Transition to the social assistance upon exhausting entitlement to unemployment benefits (single adult person, 1 member household, November 1996)

Initial Net wage ²	Percent of MLS	Unemployment income by source last 3 months of entitlement (CZK)			Replacement rate w.r. to the initial net wage,	Unemployed, UB entitlement exhausted, income from SA	Replacement rate w.r. to the initial net wage
(CZK)	%	UB	SA	Total	%	(CZK)	%
2168	75	1084	1806	2890	133 ¹	2890	133
2890	100	1445	1445	2890	100	2890	100
3613	125	1807	1083	2890	80	2890	80
4335	150	2168	722	2890	67	2890	67
5780	200	2890	0	2890	50	2890	50
8670	300	4335 ³	0	4335	50	2890	33
11560	400	4335	0	4335	38	2890	25

Source: own calculations.

Notes:

¹ Any person whose total income falls below the minimum living standard is eligible for the social assistance benefits. Therefore, a person earning 75% of the MLS and having no other source of income would have in reality applied for the SA benefits. Therefore, the effective replacement rate for such a person would have been 100%.

² We assume that the reported wage is the sole source of income for this household.

³ 4,335 CZK equals 1.5 times the MLS for an adult in a 1 person household and hence represents the maximum UB level.

⁴ The economy-wide average gross wage in the second quarter of 1996 (latest figure available) was 9,119 CZK, the rough estimate of the net wage is thus about 7,100 CZK.

4. Financing the passive benefit system

All social transfers and policies are financed from the general state budget with the sole exception of health care. Nominally, these transfers are financed by the contributions from the wage bill which are split between the employers and employees. All these contributions become at present *de facto* a part of the state budget and represent a significant additional cost burden for the employers. The worker's compulsory contributions are 12.5% of his/her gross wage: 6.5% for social insurance (pensions), 4.5% for health insurance, 1.1% for sickness benefits and 0.4% for employment policies. Employers further contribute 19.5% of the wage bill for social insurance, 9% for the health insurance, 3.3% for the sickness benefits and 3.2% for employment policies. The overall burden is thus as high as 47.5% of the gross wage bill. These high mandatory payments are thought to affect significantly the competitiveness of Czech enterprises.

The possibility of separating the financing of social insurance from the state budget has been widely discussed. Proposals to this effect were advanced both by trade unions and by employers, and were backed by several political parties. The new coalition agreement signed after the June 1996 elections to the lower chamber of the Parliament includes a commitment by the coalition partners to separate financing of the pensions from the state budget into a separate pension insurance fund. Currently the budget revenue collected from the pensions contributions exhibits surpluses over the pension expenses (in

Table 5. Transition to the social assistance upon exhausting the eligibility for the unemployment benefits (A family of four, husband works, wife does not work and is not granted parental allowance, 2 children, 6 and 12 years old, November 1996)

Initial Net wage ²	Percent of household MLS	Children allowance	Overall household income	Unemployed, last 3 months of eligibility	Replacement rate w.r. to the initial household income	Unemployed after exhausting UB eligibility	Replacement rate w.r. to the initial household income
(CZK)				UB	SA & child Total allowance	(only SA)	%
4410	50	1091	5501	2205	6615	8820	160
6615	75	1091	7706	3308	5512	8820	114
7938	90	1091	9029	3969	4851	8820	98
8820	100	1091	9911	4335	4485	8820	89
11025	125	955	11980	4335	4485	8820	74
13230	150	955	14185	4335	4485	8820	62
17640	200	477	18117	4335	4485	8820	49
26460	300	0	26460	4335	4485	8820	33
35280	400	0	35280	4335	4485	8820	25

Source: own calculations.

Note:

- ¹ We assume that the man's wage is the sole source of income for this family. In the first two rows the families would have qualified for the SA benefits even while the husband was working. Their effective replacement rate would have therefore been 100%.
- ² We disregard other types of social support benefits the family could qualify for, namely the housing and travel costs benefit.
- ³ As the unemployment benefit differs from the net wage, also the children allowances when might become different. The SA tops the income formed by the UB + children allowances to the MLS of the household.
- ⁴ The economy-wide average gross wage in the second quarter of 1996 (latest figure available) was 9,119 CZK, the rough estimate of the net wage thus about 7,100 CZK.

Table 6. Transition to the social assistance upon exhausting the eligibility for the unemployment benefits (A family of four, husband works, then becomes unemployed, wife always works and earns the economy-wide average wage of 7,100 CZK per month, 2 children, 6 and 12 years old, November 1996)

Initial Net wage of the husband	Percent of household MLS	Joint net earnings of both partners	Children allowance	Overall household income	Unemployed husband, last 3 months of entitlement Income support by source	Replacement rate of an income support w.r. to joint earnings	Unemployed husband after exhausting UB, Income Support from (SA & child allowance & wife's income)	Replacement rate w.r. to the initial overall income
(CZK)	%	(CZK)			UB of the husband	%		%
					child allowance	Total family income		
4410	50	11510	955	12465	2205	1091	10396	72
6615	75	13715	955	14670	3308	955	11363	60
7938	90	15038	955	15993	3969	955	11424	55
8820	100	15920	477	16397	4335	955	12390	54
11025	125	18125	477	18602	4335	955	12390	47
13230	150	20330	477	20807	4335	955	12390	42
17640	200	24740	477	25217	4335	955	12390	35
26460	300	33560	0	33560	4335	955	8820	26
35280	400	42380	0	42380	4335	955	8820	21

Source: own calculations.

Notes:

¹ We assume that the wages of adults are the sole source of income for this family.

² We disregard other types of social support benefits the family could qualify for, namely the housing and travel costs benefit.

³ As the unemployment benefit differs from the net wage, also the children allowances when might become different. The SA tops the income formed by the UB + children allowances to the MLS of the household. The sum of the UB, children allowance and wife's wage (10,390 CZK) exceeds the household MLS even in the first row, hence in this construction no case implies SA benefits eligibility while the husband is eligible for the UB.

1995 estimated at 2 billion CZK) but due to the ageing of the population and only a moderate increase in the retirement age, these surpluses are expected to vanish in the coming years. Currently, the surpluses are used to finance other types of social transfers.

All of the schemes described in Section 2, and indeed all social programs, except the health care, are administered by state bodies whose directors are appointed by the minister of labour and social affairs. There are no special separate supervisory bodies. All the eligibility decisions and disbursement of the social support benefits are administered by the district-level state administration in the case of social support benefits and municipalities in the case of social assistance benefits.

The majority of the expenses related to social assistance are financed from the district- (municipality-) level budgets. Part of them is covered by the district authority's revenue and the rest by the lump-sum subsidy from the state budget. The actual spending on non-mandatory items (maintenance of social care institutions, investments, etc.) is controlled exclusively by the local authority and the central government has no influence on the way the subsidy from the central budget is being spent as long as the spending covers social assistance-related expenses. Investment expenditures related to, for instance, the construction of institutions caring for the aged and disabled are typically covered from the local budgets. Expenditures on social assistance and social support benefits are practically fully covered by the central subsidies. Each district authority is assigned a special account at the Central Bank, which is used for the disbursement of the benefits, and is provided with as much funds as is needed to cover the amount of benefits for which the eligibility was established. Given these rules, the funding of the programs is essentially open-ended without any upper ceiling as far as the social support or social assistance benefits are concerned. Administrative costs are split between the central authority (Ministry of Labour and Social Affairs) and the district or municipal authorities.

Part II. Characteristics of the benefit recipients

In this part of the paper we establish the characteristics of the recipients of social assistance benefits and unemployment benefits and address the following questions: To what extent are the two sets of recipients distinguishable from each other in terms of demographic characteristics or household composition? If they are identifiable by some observable characteristics, this might assist analysts in understanding why these groups are receiving different types of benefits and hence help find solutions for getting them off these schemes and into work. On the other hand, the characteristics may reflect "self selection" resulting from the incentives of the schemes. The second question addressed in this section is to what extent these support schemes create incentives that prolong unemployment? Do people in the different benefit groups have different probabilities for staying unemployed vs. leaving unemployment for a job or to exit the labour force?

5. Are recipients distinguishable by type of benefit?

As discussed above, social assistance benefits are determined by the income, size and age composition of the members of a household. Hence in order to address the question of what distinguishes social assistance recipients from others, it is necessary to carry out the analysis at the household level. However, since unemployment benefits are given to individuals, analysis of the incentive effects of this program should be carried out for individuals. In this section, we gather information on SA and UB recipients from both the existing literature on household analysis of social assistance recipients and our own analysis at the individual level using *Czech Labour Force Survey* data.

5.1 Household analysis

Data on social assistance recipients are very difficult to obtain. The major problem of data collection is that the social assistance registers are not computerised to the same extent that the unemployment registers of the district Labour Offices are. The social assistance registers contain information needed to assess the eligibility for a social benefit, hence data on educational attainment and professional status of a client and other members of a household are minimal. Household income is recorded only when a household applies for means-tested benefits. Furthermore, there is no – or at best very little – linkage between the records kept by the Social Assistance Offices and the district Labour Offices. Nation-wide or regional-level data on the structure of social assistance recipients are thus practically impossible to obtain in conventional ways. In order to be able to analyse the characteristics of the households receiving social assistance, the Czech Ministry of Labour and Social Affairs sponsored a study by the Research Institute of Labour and Social Affairs. This section presents some fragmentary evidence obtained by the survey carried out by this institute in 1993–1995.¹⁸

The major problem of the survey, which is well acknowledged by the authors, is the non-random nature of the sample. The survey was carried out in only three districts of the country (Mladá Boleslav, Louny and Havlickuv Brod). These districts have “average” demographic structure (in terms of the age and economic activity of the population) and their choice ensured that the resulting sample contained respondents from both industrialised and agricultural districts as well as from districts with average (Havlickuv Brod), below-average (Mladá Boleslav) and above-average (Louny) unemployment rate. These three districts were also selected for the higher quality of their registered data. The sample selection ensured that recipients of each type of social assistance benefits would be evenly represented in the sample. This of course means that the recipients of the less common types of benefits were over-represented in the sample. The final sample included 1,002 households. Since the aggregate data on the structure of social assistance recipients are not available, it is very difficult to judge the country-wide representatives of this sample.

The results of the survey shows that families with an unemployed member and who are receiving social assistance tend to have a woman (usually the

¹⁸ The following text is based on Kucharova and Lhotska (1993), Kucharova and Petrova (1995).

wife) registered: about 78 percent of the registered recipients are female. This reflects the fact that a woman is typically applying for the benefits on behalf of her household. The recipients cannot be distinguished from the rest of the population by their age. However, their educational attainment is very low. Some 60 percent of the recipients have completed only primary education (9 years) and 25 percent have an apprenticeship training, without taking the final examination.

Despite the fact that at the time when the survey was carried out the unemployment rate was 3.1 percent in Havlickuv Brod and 7.1 percent in Louny, the frequency with which families quoted unemployment as the (main) explanation for being on welfare benefits was similar in the two districts. One reason is probably that unemployment per se is not the exclusive cause for falling into the social safety net. In 83 percent of the households another factor besides an unemployed member was present, the most common secondary reasons were: low income of a partner (13 percent), disabled or very old member of a household (13 percent), incomplete family (15 percent).

There is a subgroup that is very dependent on social assistance. Almost one-fifth (18 percent) of the sample had registered more than once for social assistance. Within the 'current' registration, 11 percent of the sample had been registered for over two years and another 37 percent had been registered for one to two years. One-fifth of the households had two or more members unemployed; these households were more than likely totally dependent on social assistance.

About 72 percent of the households with an unemployed member and receiving social assistance benefits were simultaneously collecting unemployment benefits. The unemployment benefits was a significant portion of total household income (31 percent) and it formed on average 54 percent of the social income of the household. These households were generally more dependent on social assistance and had lower incomes than the average household in the sample. Social assistance comprised over half (57 percent) of the household income of the households with an unemployed member and only one-third of the income of all households. The average total household income – including social assistance and unemployment benefits – for households with an unemployed person was 6,605 CZK whereas the average total income for all households receiving social assistance was 7,053 CZK. The average per capita income was 1,894 CZK (2,272 CZK respectively).

5.2 Individual analysis

5.2.1 *Descriptive analysis*

In this section we analyse the characteristics of unemployed individual receiving social assistance vs. unemployment benefits using the *Labour Force Survey* (LFS) data (as opposed to the administrative data of those registered as unemployed in the district Labour Offices).¹⁹ Following the International Labour Office guidelines, we classify an individual as unemployed if he/she is:

¹⁹ These surveys have been administered by the Czech Statistical Office at quarterly intervals since the summer of 1993 and cover approximately 1% of the households in the Czech Republic.

Table 7. Distribution of the population aged 15 + years by employment status (percentage)

	1994		First Quarter of: 1995		1996	
Employed	61.2	–	60.6	–	60.7	–
Unemployed	2.5	–	2.5	–	2.1	–
– Registered at DLO	(1.56)	100.0	(1.49)	100.0	(1.67)	100.0
Unemployment Benefit		23.1		19.0		18.4
Social Assistance Benefit		35.0		41.3		43.4
No Benefits		41.9		39.7		38.2
– Not registered at DLO	(0.94)	–	(1.01)	–	(0.83)	–
Out-of-the L.F.	36.3	100.0	36.9	100.0	37.2	100.0
students		21.2		22.4		22.4
women on leave		5.7		5.8		6.5
old age pensioners		64.9		60.2		58.4
disability pensioners		4.8		8.6		8.9
other		3.4		3.0		3.9
Total (%)	100.0		100.0		100.0	
Total ¹	8,303		8,360		8,397	

Source: Czech Labor Force Survey, weighted full sample

¹ Population of age 15+ number in thousands

a) not working in any paid job during the week prior to the survey week and b) seeking work during the last 4 weeks prior to the survey and c) ready to take a job within the next two weeks. Naturally, some portion of these unemployed are registered in the district Labour Office (LO). We begin by presenting calculations of the incidence of unemployment in the working age population using the LFS data and the ILO definition of unemployment. We also show the proportions of the unemployed that are registered and not registered at the district LO. We then show the relative prevalence of unemployment benefits (UB) vs. social assistance (SA) among the unemployed that are registered.²⁰ We finish the section with an analysis of the demographic characteristics of each group to learn to what extent they differ and hence address the question: can an individual's characteristics be used to predict which benefit group he/she is in?

Table 7 presents the distribution of the working age population (15 years and over) by labour force status in the first quarters of 1994, 1995 and 1996. It shows that the stock of unemployed people represented only between 2.1 and 2.5 percent of the working age population over this period. The shares of the population that were employed or out-of-the labour force remained fairly constant (about 61 and 37 percent, respectively). Thus the trends which were observed over 1990–1993 – declining proportion of employed and rising proportion out-of-the labour force – seems to have stabilised in 1994–1996. (See OECD, 1995, pp. 14–17 for the 1990–1993 figures.)

As seen in Table 7, the vast majority (about two-thirds) of the unemployed are registered in the district LO in 1994 and 1996. (The proportion declined

²⁰ Although we know that it is possible to receive UB and SA simultaneously, the *Labour Force Survey* question does not allow people to answer that they are receiving more than one type of benefit. Hence, a person answers that they are either receiving SA or UB.

somewhat 1995.) Of those that were registered, between 18 and 23 percent received unemployment benefits, between 35 and 43 percent received SA and about 40 percent (38–42 percent) did not receive benefits. With the expansion of eligibility for unemployment benefits and the contraction of eligibility for social assistance (due to more means testing) in January 1996, one would expect there to be a slight redistribution of people toward unemployment benefits and away from social assistance in 1996 as compared to 1995 or 1994. However, the data in Table 7 do not support this hypothesis.

The relative shares of registered unemployed by benefits type are affected greatly by the duration of the unemployment spell.²¹ For those who are unemployed for six months or less (short term unemployed) almost one-third are receiving UB whereas for the longer term unemployed, only 8 to 14 percent are receiving UB. A little more than one-quarter of the shorter term unemployed are receiving SA whereas among the longer term unemployed this share rises to over one-half. The proportion not receiving any benefits is larger for the short term unemployed (40–45 percent) than for the longer term unemployed (36–38 percent). Not surprisingly, there is an increase in the proportion that receive SA as the length of the unemployment spell passes six months since UB entitlement is for only six months. However, it is not evident why the proportion with no benefits seems to be higher in the first six months. We speculate that these are people who have not applied and/or are not eligible unemployment benefits in their first months of unemployment (because they received severance pay, etc.). This group seems to be larger than the group that has exhausted UB after six months of unemployment and is not be eligible for SA.

Returning to Table 7, we note that the lion's share of the population that is out-of-the labour force is retired (pensioners). In 1990–1993 there was a substantial increase in the number of old-age and disability pensioners (131,000 people) according to the OECD (1995, p. 15). As we noted Section 2.3.2, the laws at this time allowed pensioners to work and receive pensions. During this period, disability and early retirement were used, in addition to layoffs, as a means to reducing the number of employees in firms and providing a safety net. In 1994–1996, this trend seems to have been reversed as the stock of pensioners decreased by 3,038 persons, either through death or return to the labour force.

5.2.2 Construction of panel data

In order to learn the extent to which unemployed individuals exhausted their unemployment benefits and moved onto social assistance vs. no benefits, we constructed panel data for cohorts of the unemployed using the LFS data. Since the LFS interviews two-fifths of the households in a given quarter over four consecutive quarters, it possible to construct annual panel data for individuals in approximately 11,000 households.²²

²¹ The authors are grateful to Mr. Jaroslav Kux for pointing out that in the previous version of this paper, the missing values referred to unemployed who were not registered in the district Labour offices.

²² The quarters are as follows: 1Q = November–January; 2Q = February–April; 3Q = May–July; 4Q = August–October.

The analysis in the following two sections is carried out on panel data for two cohorts of unemployed: one that entered the LFS sample in the first quarter of 1994 (449 individuals) and the other that entered the LFS sample in the first quarter of 1995 (512 individuals). We follow these individuals from the first quarter until they leave unemployment or until the fourth quarter of the year, whichever comes first. Since 68 (64) percent of the 1994 (1995) cohort left unemployment for either employment or out-of-the labour force by the end of the year, it is not surprising that the average number of quarterly observations per individual is 3.05 (3.10) in 1994 (1995).²³

We categorised the number of changes in types of benefits observed among these two cohorts. We found that 80.3 percent and 84.5 percent of the respective 1994 and 1995 cohort samples did not change benefit or registration status over the period we observed their unemployment spell. This includes approximately one-third of the sample in each year that was 'not registered' at a district Labour Office. Between 15 and 17 percent changed status once and only 1 to 2 percent changed status twice. Among those who changed status, the most prevalent pattern was movement from receiving social assistance to not receiving benefits.

We were particularly interested in analysing the group that moved from unemployment benefits to social assistance. Unfortunately, only 1.4 percent in 1995 and 4.0 percent in 1994 were observed making this transition. Given the small sample size, we concluded that it was not possible to analyse this group separately. However we note that if this is representative of the total population, these results imply that a very small percentage of those with unemployment benefits move on to social assistance benefits in a given year.

In Table 8, we present the means (and standard deviations) of selected demographic and unemployment-related characteristics during the first quarter for each of the two cohorts. The data is stratified by registration status and benefit category. Except for the unemployment rate, which is taken from district level administrative data, all of the characteristics are available from the LFS. The means in Table 8 indicate that for both years these four groups are not strikingly different. For example, there are no significant differences between the average age and average educational level of the people in these four groups. There are some differences in terms of gender and marital status: Although married women represent a much higher proportion of the people in all categories, they are an even larger share of the individuals in the 'registered and receiving no-benefit category' – 48 percent in 1994 and 36 percent in 1995.²⁴ The characteristic that most clearly distinguishes the four categories is, obviously, the duration of unemployment.²⁵ The average unemployed person receiving unemployment benefits has unemployment spells of about 4 months (4.6 in 1994 and 4.3 in 1995) whereas those receiving social assistance benefits are unemployed for about 11 months (10 in 1994 and 13 in 1995). Clearly if most people begin their unemployment spell receiving unemployment benefits, then only the longer term unemployed will receive social assistance. The mean district unemployment rate does not seem to vary across

²³ We have a minimum of two quarterly observations per person – the first and second quarter of each year. If the individual exited in the second quarter, two is the total number of observations we have. If he/she exited in the third quarter we have three quarterly observations, etc.

²⁴ The values in the table are presented as proportions.

²⁵ Note this includes the mean duration of both completed and censored spells of unemployment.

Table 8. Characteristics of cohort samples of unemployment, by benefit category¹

	1994		1995	
	Mean	Std. Dev.	Mean	Std. Dev.
Unemployment Benefits Recipients				
Age	29.653	10.108	30.906	10.068
Education	11.056	1.537	11.531	1.894
Married men	0.083	0.278	0.109	0.315
Married women	0.403	0.494	0.328	0.473
Single women	0.181	0.387	0.281	0.453
Single men	0.333	0.475	0.281	0.453
Duration of unemployment	5.063	3.707	4.641	2.616
Unemployment rate	4.869	1.638	4.406	1.966
Proportion of dependents	0.271	0.244	0.285	0.254
of unemployed	0.308	0.179	0.292	0.151
of retired	0.121	0.197	0.051	0.154
No. of observations	72		64	
Social Assistance Recipients				
Age	30.875	10.397	33.175	10.673
Education	10.656	1.420	10.278	1.588
Married men	0.156	0.365	0.151	0.359
Married women	0.292	0.457	0.333	0.473
Single women	0.292	0.457	0.238	0.428
Single men	0.260	0.441	0.278	0.450
Duration of unemployment	10.656	8.268	13.429	9.017
Unemployment rate	4.760	1.905	4.534	1.594
Proportion of dependents	0.309	0.257	0.304	0.275
of unemployed	0.306	0.163	0.272	0.172
of retired	0.106	0.202	0.093	0.201
No. of observations	96		126	
No-Benefits				
Age	32.752	11.643	35.072	11.853
Education	10.966	1.814	10.883	1.488
Married men	0.154	0.362	0.252	0.436
Married women	0.496	0.502	0.360	0.482
Single women	0.171	0.378	0.171	0.378
Single men	0.179	0.385	0.216	0.414
Duration of unemployment	6.252	6.826	8.752	8.095
Unemployment rate	4.233	2.029	4.091	1.853
Proportion of dependents	0.254	0.245	0.259	0.243
of unemployed	0.283	0.160	0.301	0.188
of retired	0.100	0.201	0.079	0.188
No. of observations	117		111	

benefit groups. However, it is striking that the non-registered individuals tend to live in regions with much lower unemployment rates (on average) than people with unemployment benefits or social assistance benefits. We created three 'household characteristic' variables for each individual: the ratio of the number of household members who are either dependants pensioner, or unemployed to the total number in the household. Dependants include children less than 15 years of age and spouses that take stay at home taking care of the family. What is remarkable, and consistent with the structure of the

Table 8. Continued

	1994		1995	
	Mean	Std. Dev.	Mean	Std. Dev.
	Not-registered at DLO			
Age	33.494	14.487	34.142	14.625
Education	11.366	2.078	11.256	2.059
Married men	0.201	0.402	0.199	0.400
Married women	0.317	0.467	0.308	0.463
Single women	0.268	0.444	0.185	0.389
Single men	0.213	0.411	0.308	0.463
Duration of unemployment	6.366	6.794	7.543	7.588
Unemployment rate	3.011	2.137	3.226	2.155
Proportion of dependents	0.303	0.266	0.256	0.282
of unemployed	0.199	0.194	0.218	0.183
of retired	0.169	0.298	0.182	0.321
No. of observations	164		211	

Source: Czech Labor Force Survey

¹ Characteristics in the 1st Quarter

Explanation of variables:

age	– in years
education	– in years
married and single man and women	– proportion of sample
duration of unemployment	– in months
unemployment rate	– quarterly district level
household characteristics	– proportion of household
dependents	– students + children + women on maternity

benefit system, is that those who do not receive benefits have families with fewer dependants, fewer unemployed, and fewer retired persons.

We proceed below to estimate multinomial logits in order to learn if once the other characteristics are held constant, we can have a sharper picture of who is more likely to receive benefits.

5.2.3 Logit analysis

To what extent do personal and household characteristics and district labour demand determine whether an unemployed person is receiving unemployment benefits, social assistance benefits, or no benefits? To address this question we estimate a logit equation with data on the first observation of each of the two cohorts of unemployed persons. The left-hand-side variable has three categories: 1) recipient of unemployment benefits, 2) recipient of social assistance benefits; 3) non-recipient of any benefit (which is used as the base). As explanatory variables we have included:

- Demographic characteristics
 - age (years),
 - age squared,
 - education (years),
 - dummies for a combination of marital status and sex to yield: married men, married women, single men (the base) and single women,

- The duration of unemployment (in months),
- A demand variable: the quarterly district unemployment rate (in percent)
- Household characteristics:
 - the number of dependants (children under 15 years of age and housewives) divided by the number of members in the household,
 - the number of unemployed in the household divided by the number of members in the household,
 - the number of retired/pensioners in the household divided by the number of members in the household.

As is well known, the interpretation of the logit coefficients is not straight forward and is best thought of as capturing the relative likelihood of being in each state. The marginal impact of a single explanatory variable on the probability can have a different sign than the coefficient. Hence in order to aid our understanding of the relative impact of various factors, we present the estimates of both the coefficients and marginal impacts evaluated at the sample mean transition probabilities.

Tables 9 and 10 provide the means, coefficients and marginals (estimated at the means for the continuous variables and at 0–1 for the dummy variables) for the 1994 and 1995 multinomial logits predicting which benefit group someone is in. Non-recipients have been used as the base comparison group. Overall, the coefficients indicate that there are significant differences in the characteristics of unemployment benefit recipients and non-recipients and in the characteristics of those receiving social assistance versus no benefits. The estimated marginals presented in Table 9 suggest that in 1994 and 1995, a person is more likely to be an unemployment benefit recipient (compared to a non-recipient of any benefits) if he/she is younger (although the impact of age is quite small), more educated, single, with shorter unemployment spells and living in districts with higher unemployment rates. With regard to the household characteristics, in 1994 (but not in 1995) unemployed people in households with a higher proportion of dependants and unemployed tended to receive unemployment benefits. The proportion of retired members does not seem to be a determining factor in either year. In 1995 the only significant household characteristic is the proportion of unemployed members and its effect is negative on the probability that the individual is receiving unemployment benefits.

The estimates in Table 10 indicate that one is more likely to be a social assistance recipients than a non-recipient in 1994 if one is older, less educated, has longer unemployment spells, and has proportionately more dependants and unemployed members in the household. In 1995 none of the demographic characteristics mattered, nor did the duration of unemployment and the unemployment rate. The only significant determining factors in 1995 were household characteristics: those unemployed in households with proportionately more unemployed, dependants and retired people having a much higher probability of receiving social assistance.

The base probabilities for each group are presented at the bottom of Tables 9 and 10. To find the probability for any group or change in a characteristic, one simply needs to add the marginals of that group or characteristic. For example, the base probability is the probability that a single man with average characteristics receives unemployment benefits is 0.260 (0.174) in 1994 (1995). The probability that this single man would receive social

Table 9. Multinomial logit model of unemployment benefits recipients vs. registered non-recipients 1994 and 1995 (standard errors in parentheses)

Variable	1994			1995		
	means	coeff.	marginal	means	coeff.	marginal
Constant		-4.841 ^b (2.337)			-5.941 ^a (2.301)	
Age	31.337	0.190 (0.129)	0.0011	33.392	0.173 (0.124)	0.0008
Age ²	1100.263	-0.003 (0.002)		1237.266	-0.003 (0.002)	
Education (yrs.)	10.884	0.082 (0.103)	0.0113	10.767	0.250 ^b (0.102)	0.0497
Married men ¹	0.137	-2.233 ^a (0.725)	-0.3154	0.179	-1.376 ^b (0.664)	-0.1137
Married women ¹	0.404	-1.600 ^a (0.550)	-0.1508	0.342	-0.539 (0.512)	-0.0237
Single women ¹	0.214	-0.809 (0.521)	-0.1749	0.223	0.488 (0.483)	0.0648
Duration	7.435	-0.059 ^c (0.032)	-0.0190	9.836	-0.116 ^a (0.034)	-0.0215
Unemployment rate	4.571	0.174 ^b (0.086)	0.0265	4.343	0.210 ^b (0.097)	0.0218
Proportion in family of dependents	0.277	1.639 ^c (0.896)	0.1465	0.283	0.645 (0.878)	-0.0287
unemployed	0.297	2.210 ^b (1.089)	0.2054	0.287	-0.173 (1.084)	0.0402
retired	0.107	0.733 (0.923)	0.1466	0.079	-0.767 (1.181)	-0.1827
No. of observations ²		285			301	
Log likelihood		-272.86			-269.70	

Data Source: 1994 and 1995 quarterly Czech Labor Force Survey.

NB: The base probability of being an unemployment benefit recipient is 0.2603 (0.1737) in 1994 (1995).

¹ Single men are the base.

² Sample excludes unemployed not registered at DLO's.

^a Significant at the 1% level.

^b Significant at the 5% level.

^c Significant at the 10% level.

welfare benefits is 0.406 (0.451) in 1994 (1995). Hence the probability that this single man is not receiving any benefits in 1994 (1995) is 0.334 (0.375). Single men with mean characteristics (31 years of age, 11 years of education, 4.5 months of unemployment, etc.) are most likely to receive social assistance, somewhat likely to have no benefits but they are unlikely to be receiving unemployment benefits. We conclude that the personal and/or household characteristics of the unemployed, as well as the duration of their spell are important determinants of benefit status. The next question we address is whether unemployment benefits or social assistance have negative work incentive effects.

Table 10. Multinomial logit model of recipients of social welfare vs. registered non-recipients 1994 and 1995
(standard errors in parentheses)

Variable	1994			1995		
	means	coeff.	marginal	means	coeff.	marginal
Constant		-5.706 ^a (2.169)			0.049 (1.853)	
Age	31.337	0.248 ^b (0.116)	0.0037	33.392	0.069 (0.090)	-0.0011
Age ²	1100.263	-0.004 ^b (0.002)		1237.266	-0.001 (0.001)	
Education (yrs.)	10.884	0.042 (0.098)	0.0016	10.767	-0.176 ^c (0.095)	-0.0632
Married men ¹	0.137	-1.085 ^c (0.615)	-0.0255	0.179	-1.071 ^b (0.517)	-0.1575
Married women ¹	0.404	-1.489 ^a (0.530)	-0.1899	0.342	-0.686 (0.437)	-0.1276
Single women ¹	0.214	0.181 (0.474)	0.1292	0.223	0.068 (0.421)	-0.0215
Duration	7.435	0.072 ^a (0.023)	0.0237	9.836	0.062 ^a (0.018)	0.0244
Unemployment rate	4.571	0.066 (0.082)	-0.0024	4.343	0.107 (0.086)	0.0101
Proportion in family of dependents	0.277	1.599 ^b (0.805)	0.2125	0.283	1.550 ^b (0.721)	0.3331
unemployed	0.297	2.083 ^b (1.035)	0.2687	0.287	-0.830 (0.839)	-0.1919
retired	0.107	-0.052 (0.852)	-0.0900	0.079	0.927 (0.806)	0.2896
No. of observations ²		285			301	
Log likelihood		-272.86			-269.70	

Data Source: 1994 and 1995 quarterly Czech Labor Force Survey.

NB: The base probability of being a social welfare recipient is 0.4061 (0.4505) in 1994 (1995).

¹ Single men are the base.

² Sample excludes people with missing values.

^a Significant at the 1% level.

^b Significant at the 5% level.

^c Significant at the 10% level.

6. Unemployment duration and the probability of exiting unemployment for UB vs. SA vs. NB recipients

In this section we determine whether, an individual receiving unemployment benefits is more or less likely to leave unemployment than an individual receiving social assistance or a non-recipient, *ceteris paribus*. We distinguish between exits to a job and exits out of the labour force.

Using the entire data set for the two cohorts of unemployed (including the non-registered unemployed), we begin by calculating the probability that a person observed as unemployed in the first quarter of the year leaves unemployment by the end of the years to either employment (P_{ue}) or out-of-the labour force (P_{uo}) or stays unemployed (P_{uu}). The flows out of unemployment

were substantial during these two years: In 1994, a person who was unemployed in the first quarter had a 0.624 probability of leaving unemployment sometimes during the year for either employment ($P_{ue} = 0.491$) or out-of-the labour force ($P_{uo} = 0.133$). Similarly in 1995, the probability of exiting unemployment sometime during the year was 0.639 (with $P_{ue} = 0.467$ and $P_{uo} = 0.172$). These flows from unemployment to employment were extraordinary in light of the P_{ue} 's for other transitional economies: 0.350 for East Germany, (Bellmann et al., 1995), 0.033 for Russia (Foley, 1995) and 0.361 and 0.354 for Poland (Gora and Lehmann, 1995). This helps explain the lower unemployment in the Czech Republic as compared to these countries.

We also calculated the transition probabilities for the registered unemployed, by benefit groups for 1994 and 1995. Clearly those who were receiving unemployment benefits were more likely than the other two groups to leave unemployment for a job sometime during the year, with probabilities of 0.640 in 1994 and 0.574 in 1995. People receiving social assistance were just as likely to stay unemployed as to leave unemployment for a job (with $P_{ue} = P_{uu} = 0.426$) in 1994 however in 1995 they were more likely to stay unemployed ($P_{uu} = 0.530$) than to exit to employment ($P_{ue} = 0.326$). Those with no benefits were more likely to leave unemployment for a job (with exit probabilities of 0.480 and 0.521 in 1994 and 1995, respectively) than to stay unemployed or leave the labour force. Hence, the average person receiving unemployment benefits and the average person registered and not receiving benefits was more likely to leave unemployment for a job whereas the average person receiving social assistance was more likely to stay unemployed.

Do these transition probabilities imply that social assistance is having a negative disincentive effect and that unemployment benefits are not? Is it the level of the benefits that is having this effect or is it the characteristics of the people that are "selected" into these three categories that are driving the resulting transition probabilities? Could it be that, on average, the people receiving social assistance are less likely to obtain a job than someone receiving unemployment benefits because they are less qualified or simply have less desirable characteristics for the employer's viewpoint? In order to tease apart these two effects, one would need data on the level of benefits in each scheme as well as the characteristics of the people.²⁶

Unfortunately the LFS does not collect information on the level of benefits the individuals or households receive from UB or SA. However, we do know from the Tables 1 and 2 that families with more children tend to receive relatively higher social assistance benefits. Obviously families with more unemployed will tend to receive more unemployment benefits, and perhaps significant social assistance. Finally families with a large number of pensioners will tend to receive more pension income than families with a smaller number of pensioners. Hence, these household/family variables can be used as proxies for the relative level of the UB and SA (and pensioner) benefits among households. We can then test the extent to which an unemployed person's demographic characteristics vs. his/her household characteristics (proxies for benefit

²⁶ Inserting a dummy for which benefit category one is in into a hazard model for transition out of unemployment would thus not capture the disincentive effect of the benefit since it captures both the characteristics of the people in the benefit scheme (selection mechanism) as well as the disincentive effect.

levels) determine the probability of leaving unemployment for a job (or out of the labour force).

We have shown in Section 5.2.2 that personal and household characteristics and the duration of the unemployment spell play an important role in determining which benefit scheme a person is on. Hence we can see whether the characteristics which determine benefit identity also determine transition probabilities and hence explain the overall average transition probabilities above.

We proceed by estimating individual transitions out of unemployment (the hazards) with multinomial logits (exits to employment and out-of-the labour force) using essentially the same right hand side variables used in the benefit function. We have included two higher order terms of duration since hazards are sensitive to the specification of duration.²⁷

Table 11 provides the means, coefficients and marginals for the exits from unemployment to employment for 1994 and 1995 and Table 12 provides the same information for exits from unemployment to out-of-the labour force. The estimated coefficients for the transition from unemployment to employment in Table 11 lead us to conclude that demographic characteristics are not a stable determinant of exits from unemployment to employment. Whereas age matters in 1994, it does not in 1995. Education is not significant in either years and only one marital status-gender variable is important in one year. This would suggest that it is not the characteristics of the unemployed people that determines whether or not they get a job – i.e., both educated and uneducated, young and old, men and women, married or not have similar chances of finding employment. What is important is the structure of the household: Those with relatively more dependants, unemployed and retired persons are less likely to leave unemployment for employment (and more likely to remain unemployed). Since these are higher benefit families, it would seem that the household income is having an “income effect” on the unemployed individual. Moreover, since there is a negative duration effect and individuals with longer unemployment spells tend to be receiving SA, this could lead us to suspect that the level of household SA benefits is having an income effect (work disincentive effect) on the unemployed individuals.

The estimated coefficients and marginals in Table 12 indicate a similar finding in that the demographic variables do not play much of a role (except for age in 1995) and the duration variables are very important in determining the outflows from unemployment to out-of-the labour force. The longer term unemployed are less likely to leave the labour force. However, this time, the household composition variables are not important. Hence whether or not a person is more or less likely to receive SA or UB benefits does not affect the probability of exiting the unemployment pool to out-of-the labour force. We conclude that none of the variables that were important for explaining exits to a job are important determinants of exits to out-of-the labour force.

III. Summary conclusions

A social safety net must balance income support while still providing sufficient incentive to work for those who have a capacity to do so. In this paper we

²⁷ We tested for specification using the log likelihood ratio test with duration entered up to the power of four and found that the specification with duration up to the power of three was best fit by the data.

Table 11. Multinomial logit model of transitions from registered unemployment to employment 1994 and 1995 (standard errors in parentheses)

Variable	1994			1995		
	means	coeff.	marginal	means	coeff.	marginal
Constant		26.736 ^a (6.534)			22.962 ^a (6.124)	
Age	31.719	0.595 ^a (0.232)	0.0194	33.965	0.167 (0.179)	0.0003
Age squared	1125.572	-0.008 ^b 0.003		1279.906	-0.002 (0.002)	
Education (yrs.)	10.874	-0.312 (0.195)	-0.0711	10.768	0.166 (0.168)	0.0208
Married status ¹						
Married men	0.130	-2.480 (1.146)	-0.5080	0.171	-0.081 (1.049)	0.0058
Married women	0.400	-1.146 (0.890)	-0.2821	0.345	-1.643 ^c (0.885)	-0.2117
Single women	0.221	-0.062 (0.879)	-0.0155	0.210	-0.241 (0.844)	-0.0335
Proportion in family of dependents						
unemployed	0.273	-6.258 ^a (1.774)	-1.5430	0.281	-4.802 ^a (1.464)	-0.6873
retired	0.171	-18.918 ^a (2.818)	-4.6027	0.213	-17.431 ^a (2.249)	-2.3512
unemployed	0.114	-9.573 ^a (2.242)	-2.3396	0.085	-5.043 ^a (1.502)	0.6794
Unemployment rate	4.310	0.034 (0.152)	0.0146	4.050	0.133 (0.159)	0.0155
Duration of unemp.	12.232	-4.964 ^a (0.972)	-0.0615	15.340	-3.936 ^a (0.873)	0.0069
Duration squared	221.407	0.285 ^a (0.058)	333.978	0.209 ^a	(0.046)	
Duration cubed	5062.306	-0.005 ^a (0.001)	8710.125	-0.003 ^a	(0.001)	
No. of observations		285			310	
Log likelihood		-112.6			-127.3	

Data Source: 1994 and 1995 quarterly Czech Labor Force Survey.

Sample transition probability 0.424 (0.167) in 1994 (1995) is calculated for base.

¹ Single men are the base.

^a Significant at the 1% level.

^b Significant at the 5% level.

^c Significant at the 10% level.

have presented the structure of the social safety net and tried to measure its incentive effects.

We conclude that the unemployment benefit system in place today is parsimonious by European standards, allowing for six months of non-taxed benefits at replacement rates of 60% and 50%, and a maximum benefit that is 1.8 times the minimum living standard (MLS). One would surmise that the recent expansion of eligibility criteria to include once again people who have worked at home, taking care of family members, should increase the numbers registering for benefits in the district Labour Offices. However, as of the

Table 12. Multinomial logit model of exits from registered unemployment to out-of-the labor force 1994 and 1995
(standard errors in parentheses)

Variable	1994			1995		
	means	coeff.	marginal	means	coeff.	marginal
Constant		25.175 ^a (5.808)			21.064 ^a (5.734)	
Age	31.719	-0.156 (0.161)	-0.0005	33.965	-0.260 ^c (0.142)	0.0048
Age squared	1125.572	0.003 (0.002)	1279.906	0.005 ^b	(0.002)	
Education (yrs.)	10.874	-0.171 (0.150)	-0.0019	10.768	0.127 (0.137)	0.0095
Marital status ¹						
Married men	0.130	0.458 (0.916)	0.1042	0.171	-0.909 (0.758)	-0.0891
Married women	0.400	0.131 (0.803)	0.0403	0.345	-0.894 (0.691)	-0.0583
Single women	0.221	0.035 (0.801)	0.0031	0.210	0.003 (0.670)	0.0048
Proportion in family of dependents						
unemployed	0.273	0.488 (1.329)	0.2212	0.281	1.041 (1.099)	0.1938
retired	0.171	-0.587 (1.361)	0.5323	0.213	-3.891 ^a (1.408)	-0.0611
Unemployment rate	0.114	0.058 (1.407)	0.2928	0.085	-1.171 (1.345)	-0.0222
Unemployment rate	4.310	-0.206 (0.128)	-0.0147	4.050	0.159 (0.135)	0.0133
Duration of unemp.	12.232	-3.513 ^a (0.791)	-0.0263	15.340	-3.279 ^a (0.819)	-0.0038
Duration squared	221.407	0.167 ^a (0.041)		333.978	0.167 ^a (0.041)	
Duration cubed	5062.306	-0.002 ^a (0.001)		8710.125	-0.003 ^a (0.001)	
No. of observations		285			310	
Log likelihood		-112.6			-127.3	

Data Source: 1994 and 1995 quarterly *Czech Labor Force Survey*.

Sample transition probability 0.071 (0.085) in 1994 (1995) is calculated for base.

¹ Single men are the base.

^a Significant at the 1% level.

^b Significant at the 5% level.

^c Significant at the 10% level.

middle of 1996, there has not been a visible increase in the proportion of unemployed with unemployment benefits in the administrative data. Nor is there any evidence in the *Labour Force Survey* data of an increase in the proportion of unemployed people on unemployment benefits.

On the other hand, the structure of the social assistance and social support systems – despite many recent changes – exhibits many problematic signs in terms of the implied incentives for the recipients. The system has moved in the right direction by increasing the number of benefits that are means tested, but the level at which the MLS is set is relatively high, especially for families with

many children. The MLS for a one member household exceeded the minimum wage in 1995 and 1996. The MLS for a family of four (with two children) which had exceeded the economy-wide average wage prior to 1995, was 15% below the average wage in 1996. The relatively high standard means that a) targeting is not as narrow as might be desired; b) social transfers represent a non-trivial part of the income for families with children and c) the scheme might have a serious work disincentive effect. However, the fact that able bodied people are required to register at the unemployment office, and accept jobs offered to them, is a mechanism that prevents some free riders.

In an attempt to improve the financial strength of the pensions system, the Pension Insurance Bill, which came into effect January of 1996, has introduced incentives and regulations for individuals to remain in the labour force rather than retire early or even at the statutory retirement age.

Do the unemployed people receiving unemployment benefits (UB) have different characteristics from those receiving social assistance (SA) or no benefits (NB)? The answer to the question, based on *Labour Force Survey* data, which has its shortcomings, is yes. An unemployed person is more likely to receive unemployment benefits (compared to no benefits) if he/she is younger, more educated, single, with shorter unemployment spells, living in districts with higher unemployment rates, and having a relatively high proportion of his/her members in the household be unemployed or dependants. One is more likely to be a social assistance recipient than a non-recipient if one is older, less educated (only in 1994), has longer unemployment spells, and has proportionately more dependants and unemployed members in the household. Since the SA package is more advantageous for families with many children this finding is not too surprising.

Who are the people most likely to leave unemployment for a job? Our logit estimates show that it is not those with relatively more dependants, unemployed and retired persons in their households. They are less likely to leave unemployment for employment (and more likely to remain unemployed). Since these are also the characteristics that increase the probability of receiving social assistance and in turn determine how high the benefits are, we may conclude that the social safety net is indeed having a disincentive effect. People with large families tend to be on SA and staying unemployed for longer spells.

Appendix: The concept of income for the purpose of means testing

For the purpose of establishing eligibility for the means-tested social support benefits and social assistance benefits, a household is considered as a single entity and incomes of all the household members are added together. The household is defined as a single person, married or non-married couple (the latter under the condition of permanently living together and sharing the common household expenses for at least a year), or parents (persons replacing them) and dependent children living in a common household. Grandparents and other household members, except parents and their children, are not included. The only exception is the benefit to cover housing expenses: all persons permanently residing in a flat are considered jointly for the purpose of means testing without any further conditions.

The income for the purpose of means testing includes these broad categories:

- income from any activity (both dependent and self-employment) which is subject to the income tax, net of this tax and general social insurance, health insurance and contributions to the state employment policy
- all returns from property (including royalties etc. and capital gains from a property sale) and capital (including interest rates), net of taxes and general social insurance
- sickness benefits and pensions
- unemployment benefits
- when testing for the social assistance benefits also any welfare benefits (e.g. parental allowance
- other minor benefits (such as income of conscripts, student stipends, etc.).

The draft principles of the new Law on Social Assistance which are currently discussed by the government foresee also property testing for deciding the eligibility for the social assistance benefits. It has been proposed that both immovable and movable property would be regarded, except for a customary household equipment. Movable property would not be regarded during the first six months, and immovable property sale or lease should not lead to the loss of acceptable housing. In the current system, property is not considered for the purpose of means testing.

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