

**Unemployment in the EU and Russia:  
Management of unemployment.**

Arestov Andrey

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## 1. Introduction

This present project reveals different measures which European countries viz Germany, Italy and Russia try to apply against still increasing unemployment. In this context it would be necessary to quote Marx and Engels.

*Every child knows that a nation which ceased to work, I will not say for a year, but even for a few weeks, would perish. Every child knows, too, that the volume of products corresponding to the different needs require different and quantitatively determined amounts of the total labour of society... And the form in which this proportional distribution of labour asserts itself, in a social system where the interconnection of social labour manifests itself through the private exchange of individual products of labour, is precisely the exchange value of these products... Science consists precisely in demonstrating how the law value asserts itself.*

Marx and Engels 1975: 196: emphases in original

Many developed countries seized by high rate of unemployment on the grounds of different matters have to act in the frames of their point of view. Last decades lots of methods and ideas were applied for solving some aspects of this phenomenon. Many European countries spend millions and billions on measures of employment promotion with the explicit aim of contributing to the reduction of unemployment.

This work shows conceptions of reduction of unemployment which were applied within last four years by already mentioned states. Strong policy towards the regulation of labour market gives the country advantages in different fields in front of other states. To hold leading positions every state is ready to conduct different socio-economy measures towards stability of its national security.

Employment and unemployment are the main indicators of social state security. Since 90<sup>th</sup> the growth of unemployment in OECD countries resulted in that that countries began to apply legal and economic principles towards the leveling of normal conditions of employment. The nature of unemployment, faced by every country, is different. Youth unemployment is high in such countries as Spain, Italy and France but in Germany such figures are sufficiently low. Then in most EU countries unemployment of females is evidently higher than of males.

In comparison with the situations in the EU and Russia we can point out different grounds of unemployment. In Russia such phenomenon took place after the collapse of the USSR when different business ties and relations were cut and most of qualified staff members

and workers become unemployed. It is ought to say that the majority of former soviet citizens could not turn to the new way of relations not similar with those were in the USSR. In this transformational society no one could find one's place under such complicated conditions at once. The unemployment rose up from 6 percent in 1993 to 13.3 percent in 1998 and descended to 8.7 percent in 2003.<sup>1</sup>

Leaps of the unemployment were registered in Europe in the 1970s after the oil shocks, and after falling back in the 1980s, it rose to a new peak in the middle of the 1990s. Continuing the listing of slopes and raising of the unemployment in Europe some processes of the re-union of Europe should be noted viz in Germany, where millions of people inspired by new economic tendencies after the reunion found themselves in front of heavy economic changes and incapability to react upon it in time.

Thus for the avoidance of such matters states apply different schemes, programs for supporting employment and preventing unemployment.

## **2. Theories and programs on preventing unemployment.**

One of the earliest theoretical approach to employment security can be found in the works of Adam Smith particularly in his work the *Inquiry into the Nature and Causes of the Wealth of Nations* (1976 edition Vol. 1: 120). Smith writes:

*The wage of labour in different occupations vary with the constancy or inconstancy of employment... What he (a mason or bricklayer) earns, therefore, while he is employed, must not only maintain him while he is idle, but make him some compensation for those anxious and desponding moments which the thought of so precarious a situation must sometimes occasion... The high wages of those workmen, therefore, are not so much the recompense of their skill, as the compensation for the inconstancy of their employment.*

This concept of wage differentials assumes a division of workers into different groups on different grounds. Here one can see that the wage becomes an indicator of the level of occupation and quality of work fulfilled by a worker. For instance, occupations with more hazardous health conditions are supposed to compensate through high wages. Work with some difficulties and risks interests potential workers in high wages, different compensations or social conditions provided by employers. But there is a concept of the Nobel laureate, Ronald Coase, that shows that the principle of chose of job doesn't obey a price mechanism. He says 'If a workman moves from department Y to department X, he doesn't go because of a change in relative prices, but because he is ordered to do so' (Coase 1937: 387). To avoid such sorts of actions of employer one uses long-term work contracts and Coase stresses advantages of

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<sup>1</sup> EBRD, Transition Report

these contracts. The advantages result from the fact that contracts define the content of the work carried out.

But fixed-term employment has some negative consequences. If there is a termination of a fixed-term contract connected with employment uncertainty there is a high risk of unemployment and it reflects negatively on investments in education and further training. Hence, investments in such programs viz education and training are being reduced due to the uncertainty of employment over the entire life-cycle.

There are some correlations between education and wage for a fulfilled job (Becker 1964 and Mincer 1974). If fixed-term contracts were independent of the level of education, this should have no effect on education. But if there is a risk of unemployment after the termination of a fixed-term contract among firms which have high investments in training programs, then the returns to higher education will be reduced. And persons with low level of education obtain less labour earnings than those with higher education and in this case earnings differentials increase. Such situation with inequality in earnings among low and highly educated employees gives birth to the demand for higher education. Hence, it results in increasing gap between well-paid and stable jobs for graduates and low paid insecure jobs for those with low level of education or without some at all.

Employment stability has influence on the theory of labour market segmentation (Stinchcombe 1979, Schömann 1994). This theory distinguish primary and secondary segment jobs. Primary segment jobs imply long-term employment and career ladder. Second segment jobs mean low level of wages, instability, low level or absence of career progress and precarious employment prospects. Such unstable jobs are in specific industrial segments like textiles, wood, paper, different service sectors. There is an interrelation between fixed-term employment and employees of secondary job sector. This interrelation shows itself in that fact that employers offer for such category of workers work contracts of low level with low wages, few career prospects and no further training possibilities and employees try to avoid such long-term contract and consider it as a negative of firm's employment record. Hence, employers of secondary job segment find it very difficult to attract employees of highly skilled labour. And in this case we can see a way of increasing unemployment because of insufficient attention to the problem of low-skilled labour.

To avoid some sort of problems, which have connections with the unemployment; researches (Gregg and Manning, 1997) define some principles to carry out by countries:<sup>2</sup>

- Social security systems which provide a safety net for the living standarts of those out of work and which reduce the gap in living standards between those in or out

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<sup>2</sup> Unemployment policy. Government options for the labour market. Cambridge, 1997.P. 336

of work and are thought to reduce the incentives to find or keep jobs. Where the safety net is paid by taxes on wages it will also raise total labour costs.

- Minimum wages which price workers out of jobs if set at levels above those prevailing in an unregulated labour market.
- Employment protection legislation such as restriction on the ability of employers to hire and fire at will also raise labour costs lead to reduced flexibility and possibility reduced employment.
- Trade unions which raise wages to levels which destroy jobs and perhaps reduce productivity efficiency through restrictive practice.

Some see different grounds of the problem of unemployment. According to one point of view (Minford and Riley, 1994), the rise of unemployment in the OECD since 1950s was caused by the excessively increased scope of labour market regulation, which came to 1980s. Another point of view, which was popular among different researches, pointed out combination of labour market regulation with a number of shocks like the oil price rises in the 1970s that caused unemployment. And the third point of view underlines technological change that is biased in favour of skilled labour, combined with globalization of the world economy, and has led to a deterioration in the economic position of unskilled labour in OECD countries and with labour regulations which make it difficult to apply adjustments in the wage structure. And all these aspects increase unemployment, especially among less skilled workers.

In this case, the best way to solve the problem is to apply measures of de-regulation.<sup>3</sup> This type of analysis is well summarized by the OECD Job Study<sup>4</sup> which conclude that:

*Wages have significant consequences for employment and unemployment. The process of wage determination is strongly influenced by labour market pressures, social perception, legislation and industrial relation system.*

A notion of the “flexible labour market” comes through the report, but “flexibility” has numerous of interpretations. The OECD uses the flexibility in the context of policy reforms – that wages should be highly sensitive to unemployment and that the unemployed should enter work frequently to avoid a build-up of long-term unemployment. “Wage flexibility” should mean that as unemployment rises, real wage costs should fall relative to productivity.<sup>5</sup> The same flexibility should be sensitive to concentrations of unemployment in society, if unemployment is higher for young people their wages should fall relative to older workers. This

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<sup>3</sup> “Labour market de-regulation” (or “de-regulation”) – is the term that refers to the type of policies which have their aim the reform of social security system to make benefit provision less generous, the reduction or abolition of minimum wages, the removal of employment protection and reductions in the power of trade unions. (Unemployment policy. Government options for the labour market. Cambridge, 1997.P. 337)

<sup>4</sup> OECD, 1994. P. 22

<sup>5</sup> Unemployment policy. Government options for the labour market. Cambridge, 1997. P.338

would impel employers to recruit young people. These measures should help to avoid long-term unemployment and as a consequence a deprivation and waste of usable skills and motivation.

Another point of view (Layard, 1997) exposes a monetary scheme against long-term unemployment and possible motivation for job search and work. Layard writes, that one of the way is to reduce the duration of benefits for one year and whereupon the state stops paying anything at all. But at the same time the state takes a responsibility to find a work for an unemployed for at least six months. Unemployed in his turn must define what he wants, to stay and receive a pecuniary aid with strict limits or get a job with further benefits and advantages. The scheme of the second decision goes thus:<sup>6</sup>

1. After the 12<sup>th</sup> month, it would relieve the public finances of any responsibility for people who are already in work. It is very difficult to prevent fraud without being able offer full-time work.

2. Between months 12 and 18, people would be producing something rather than nothing.

3. And the biggest effect would come after 18<sup>th</sup> month. Provided the temporary work had been real work with regular employers, unemployed people would have re-acquired work habits plus the ability to prove their working capacity. They would have a regular employer who could provide a reference – or retain the individual on a permanent basis. The main justification for the proposal is not that it employs people on a subsidized basis but it restores them to the universe of employable people.

It is important to mention and financial aspects of the program. Layard suggest another one scheme:

1. After the 12<sup>th</sup> month the taxpayers stop supporting those who are already fraudulently in work.

2. Between the 12<sup>th</sup> and 18<sup>th</sup> month, the taxpayers keep paying benefit but now it goes to employers not workers. However an employer who would anyway have gired somebody unemployed between 12 and 18 months will claim the subsidy, so that there would on this account be some deadweight – extra expenditure.

3. After the 18<sup>th</sup> month, there will be major savings on benefits and extra taxes received. On any reasonable estimate the total of all these will be a positive saving to the government, and a saving higher than the extra cost of the Employment Service.

All these measures could be summed up by a statement:

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<sup>6</sup> Unemployment policy. Government options for the labour market. Cambridge, 1997. P.336

*Job subsidies without compulsion to accept an offer can easily be ineffective.*<sup>7</sup>

The schemes, mentioned above, could be applied to active labour market policies, which are in fashion. The OECD describes active labour market policies as measures which “improve the labour market and jobs; develop job-related skills; and promote more efficient labour markets”.<sup>8</sup> But there is a contrary term “passive policies”. Some times it is hard to distinguish “active” and “passive” policies, but the main idea of these policies is direct or indirect subsidies. For example, direct employment subsidies are counted as ALMP (Active labour market policy), while subsidies to nationalized industries are not. Measures to encourage unemployed to compete more effectively for jobs are in the ALMP category, while changes in trade union law or competition policy are not.<sup>9</sup>

The OECD picks out five main types of ALMP: subsidized employment, direct job creation, labour market training, public employment services and youth measures. All these measures are aimed at improvement of conditions for unemployed jobseekers. Of course, some measures have pitfalls. If we take training schemes we can find it in some cases short-sighted, because it needs great expenditures to conduct such trainings in every time developing world. But if we look at this problem from the place of unemployed person we could find that on completion of such training program it is more likely to find a job or find something better-paid and it is less likely that those reenter unemployment.

It is important to refer to the main principles. The OECD suggests nine principles of policy which should combine with a reasonable level of unemployment:

1. Macroeconomic policy should be set to encourage sustainable growth.
2. Technical development should be encouraged, as should its diffusion into the economy.
3. Flexible working time, both in current hours and amount of lifetime in the labour force, should be encouraged.
4. A positive entrepreneurial climate to encourage business start-ups should be generated.
5. Wages and non-wage labour costs should be made more flexible across groups in the workforce, especially for the young.
6. There should be reform of employment security provision.
7. Active labour market expenditure should be increased instead of passive benefit provision.
8. Workforce skills should be improved through education and training programmes.

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<sup>7</sup> Ibid. P. 338

<sup>8</sup> OECD, 1994.

<sup>9</sup> Thomas Lange Unemployment in theory and practice. Cheltenham, 1998. P. 145.

9. Unemployed benefit systems (and tax) should be reformed to encourage positive incentives to go into work.

### **3. State regulation**

#### **3.1 Germany**

##### **3.1.1 Labour market in Germany**

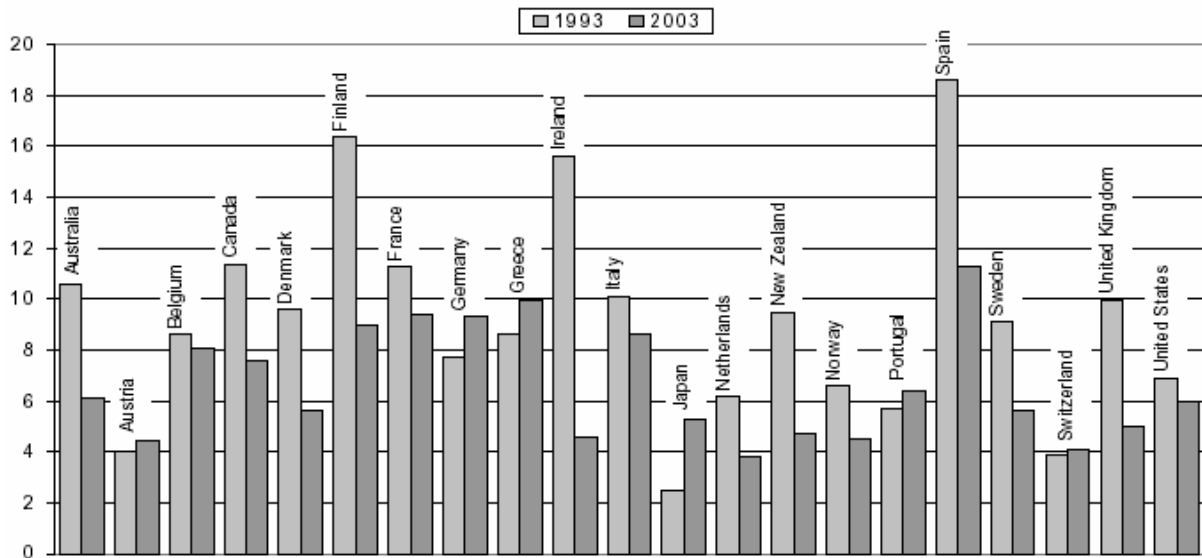
Almost 15 years after Unification in 1990, Germany is still struggling with the economic consequences of this event. Although the East German economy has made considerable progress since its near-collapse after the German monetary, economic and social union in July 1990, the East German labour market has not yet recovered. Quite to the contrary, unemployment has doubled from 10 per cent in 1991 to 20 per cent in 2004 and has become increasingly persistent as indicated by rising incidence of long-term unemployment. Western Germany, after a short post-unification boom in the early 1990s, is still struggling with the financial burdens of German Unification. The recovery of the East German economy in the early and mid 1990s has been induced and sustained by huge money transfers from the West to the East.<sup>10</sup> In addition, a substantial part of the initial cost of East German unemployment was, in fact, borne by Western Germany. In 1990, the rather generous Western social insurance system had been extended to the former German Democratic Republic (GDR) which did not have a comparable system, so that initial funding for activation measures and benefit payments had to be provided by West German social insurance. Even today, substantial transfers from the West to the East are used to prevent the already weak East German economy and labour market from further deterioration. The high cost of German Unification together with an unfavourable state of the world economy in the early 1990s which depressed German exports, had negative impacts on the West German economy and labour market. As a result, unemployment rose and became increasingly persistent in Western Germany as well. Today, Germany is one of the very few OECD countries with higher unemployment than close to the peak of the world recession in 1993 (see Figure 1). During East German transition from a centrally planned to a market economy, active labour market policy (ALMP) has become one of the most important economic policy instruments of the German Federal Government. In 1991, about one third of the East German labour force had participated in some ALMP measure (BA, 1992a). In the period 1991 to 2002, Germany has spent between 1.2 and 1.7 per cent of its GDP on ALMP (OECD, 2004b,c). Also, with increasing levels and persistence of unemployment, expenditure for income support during unemployment has risen to 2.1 per cent of GDP in 2002. In total, Germany has spent 3.3 per cent of its GDP on labour market policy in 2002. Of the 21 OECD countries included in Figure 2,

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<sup>10</sup> In the period 1991 to 1999, between 4.1 and 5.4 per cent of West German GDP went to Eastern Germany in the form of public transfers (Wurzel, 2001).

only Denmark, Belgium and the Netherland had higher expenditure. In response to exploding cost of unemployment and continuing public pressure to solve the unemployment problem, the

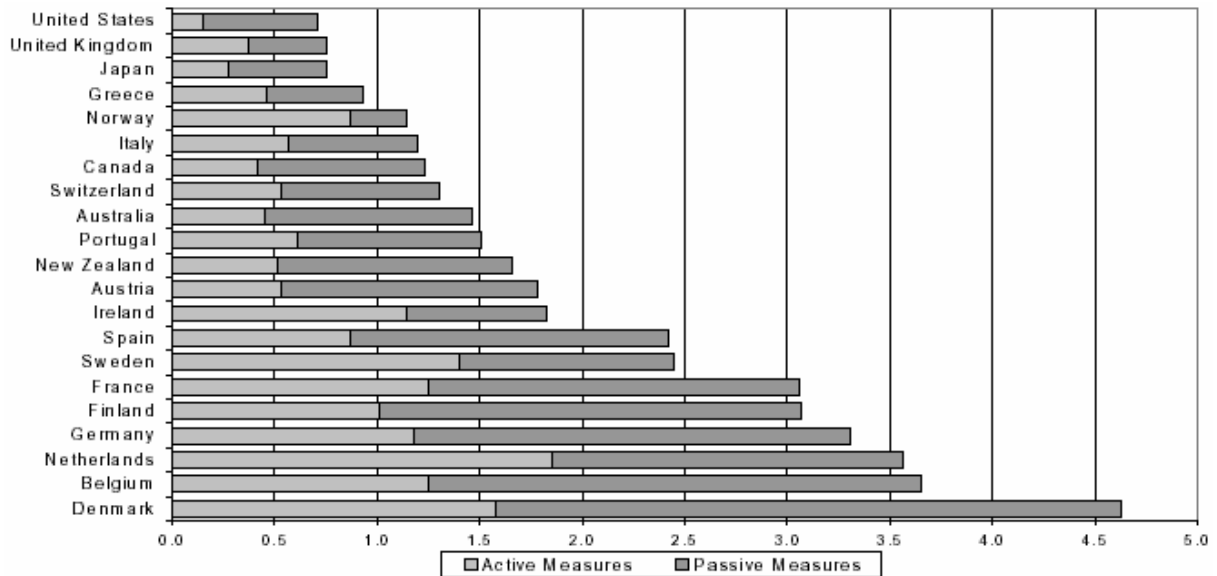
**Figure 1: Standardised unemployment rates in 21 OECD countries 1993 and 2003**



Note: Unemployment as a percentage of the total labour force. Greece: 1993 and 2002. Source: OECD (2004b).

German Federal Government has started the largest social policy reform in the history of the Federal Republic in 2002. Substantial labour market and welfare reforms had taken place earlier in several other OECD countries with high unemployment rates in the early 1990s, e.g. in Australia, Finland, Ireland and the United Kingdom. These countries have succeeded to lower their unemployment rates considerably (see Figure 1).

**Figure 2: Expenditure on active and passive measures in 21 OECD countries 2002**



Note: Expenditure as a percentage of GDP. United States, Japan, Canada, Australia, New Zealand fiscal year 2001-02, United Kingdom 2002-03, Greece 1998, Ireland 2001. Source: OECD (2004b).

### 3.1.2 German Labour Market after Unification

In 1989, the centrally planned economy of the German Democratic Republic (GDR) was characterised by a capital stock and production technologies that were largely obsolete by Western standards, an industry structure that was biased in favour of agriculture and manufacturing and against services, as well as strong dependency on exports to the CMEA<sup>11</sup> countries. Almost 55 per cent of the GDR's industry equipment was older than 10 years and more than 21 per cent older than 20 years. Agriculture, forestry, energy, mining and manufacturing accounted for 47 per cent of employment compared to only 37 per cent in Western Germany. Almost 73 per cent of the GDR's exports went to CMEA countries.<sup>12</sup> Moreover, most of the GDR's goods were produced for the sheltered domestic and CMEA market only. Thus not being exposed to open competition in the world market, product quality was frequently low. The GDR had a labour force of about 10 million people in 1989 and unemployment was almost non-existing.<sup>13</sup> Western Germany, in contrast, was a modern market economy with a labour force of about 28 million people and an unemployment rate of 7.9 per cent in 1989 (BA, 2001).

The German monetary, economic and social union on July 1, 1990, introduced the Deutschmark in the GDR, replaced all trade, capital and labour movement barriers between Eastern and Western Germany, and harmonised their legal, tax and social insurance systems. Within days a severe price-cost squeeze became apparent (Akerlof et al., 1991). Because contractual wages were converted into Deutschmarks at par and contracts remained unchanged in

<sup>11</sup> The Council for Mutual Economic Assistance (CMEA) was an organisation for the economic cooperation of the communist countries Soviet Union, Bulgaria, Czechoslovakia, GDR, Hungary, Romania, Poland, Cuba, Mongolia and Vietnam, which had existed from 1949 to 1991.

<sup>12</sup> All numbers are taken from Siebert (1991).

<sup>13</sup> However, estimates of hidden unemployment range from 15 to 30 per cent (BA, 2001).

nominal terms while - in response to intensified competition - nominal producer prices were roughly halved, real wage costs approximately doubled in July 1990. In contrast, the ratio of gross wages to the cost of living remained almost unchanged. In addition, East Germans began to substitute Western products for domestic goods on a massive scale. As a consequence, industrial output declined by 35 per cent in the same month, a phenomenon which affected every major industrial sector and virtually every commodity (Akerlof et al., 1991). Output declined further as CMEA countries were no longer able to pay the effectively tripled prices of East German goods and new buyers could not be found given the lack of world market competitiveness of most products (BA, 2001). By December 1990, production of goods had dropped to 46 per cent of its 1989 level (Akerlof et al., 1991). This had strong adverse impacts on the East German labour market. From 1989 to 1991 the work force declined by almost 3 million people (BA, 2001). A substantial part of these people was directly absorbed by active labour market programmes to keep the official unemployment rate - which does not include participants in ALMP - from skyrocketing. Many older people left the labour force encouraged by generous early retirement schemes. In spite of this, registered unemployment rose rapidly to a rate of more than 10 per cent in 1991 (BA, 1992a).

Western Germany, in contrast, experienced a boom directly after Unification. With substantial East German spending diverted away from domestic products to previously unavailable West German goods, production and labour demand increased in Western Germany. GDP grew 5.7 per cent in 1990 and 5 per cent in 1991 (see Table 1). Unemployment declined to a rate of 6.2 per cent in 1991 despite a significant growth of the labour force due to migration from Eastern Germany and Eastern Europe to Western Germany.<sup>14</sup> At the same time, the world economy was experiencing a recession. In 1992, this recession also began to affect Western Germany because of its large export share. Economic growth slowed down to only 1.7 per cent. Already one year later, the West German economy was deep in recession. GDP declined by 2.6 per cent in 1993 and unemployment rose to 8 per cent.

Despite a boom in the construction industry due to substantial public infrastructure investment and private building activity as well as a constantly expanding service sector which produced annual GDP growth rates of 6 to 9 per cent, the situation in the East German labour market continued to deteriorate in the mid 1990s. One reason for this was the large and only slowly narrowing gap between worker productivity and wages (see Table 1). Already in 1990, at the beginning of East German transition process, in most industries collectively bargained

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<sup>14</sup> Annual migration from Eastern to Western Germany during 1989 and 1990 amounted to about 2 per cent of the East German population (Akerlof et al., 1991).

**Table 1: Selected economic indicators for Germany 1990-2004**

Year	GDP growth <sup>a</sup>		Unemployment rates <sup>b</sup>		Productivity <sup>c</sup>	Gross wages <sup>d</sup>
	West	East	West	East	East/West	East/West
1990	5.7	-15.6	NA	NA	NA	NA
1991	5.0	-19.2	6.2	10.2	32.9	57.5
1992	1.7	6.2	6.4	14.4	35.5	67.7
1993	-2.6	8.7	8.0	15.4	39.0	74.2
1994	1.4	8.1	9.0	15.7	41.4	77.1
1995	1.4	3.5	9.1	14.8	42.5	79.1
1996	0.6	1.6	9.9	16.6	43.4	79.5
1997	1.5	0.5	10.8	19.1	44.6	79.8
1998	2.3	0.2	10.3	19.2	66.9	80.1
1999	2.1	1.8	9.6	18.7	67.7	80.9
2000	3.1	1.3	8.4	18.5	68.5	81.3
2001	1.1	-0.5	8.0	18.8	69.1	81.2
2002	0.2	-0.2	8.5	19.2	69.9	81.2
2003	-0.1	-0.2	9.3	20.1	NA	81.2
2004	1.7	1.2	9.4	20.1	NA	NA

Note: All entries are in per cent. <sup>a</sup>GDP at constant 1995 prices. The numbers for 2004 are first preliminary estimates. <sup>b</sup>Registered unemployment as a percentage of the dependent civilian labour force. <sup>c</sup>GDP per hour worked at 1995 prices. <sup>d</sup>Gross wages per employee. NA: not available. Source: Statistisches Bundesamt, BA (1992a-2004a), IAB (1998).

wages were set to reach parity with West German levels in 1994. Yet, the wage increases were completely unrelated to labour productivity which, in 1991, was only 33 per cent of the West German level. In contrast, wages were already at 57 per cent in 1991. Although average education levels were high in Eastern Germany, many were underprepared for work in a modern market economy (Akerlof et al., 1991). The human capital of many East Germans depreciated rapidly due to a completely changed demand for skills. In addition, the East German capital stock inherited from the GDR was largely obsolete by Western standards. In response to rising unemployment throughout the early and mid 1990s, collective agreements have been adapted. Achievement of wage parity has now been postponed to 2007 or later in most industries. Since 1995 relative wages have remained almost constant at about 80 per cent of the West German level (see Table 1).

In the second half of the 1990s, growth in the East German economy slowed down, mainly induced by the down-sizing of the construction industry following the continuous cut in public expenditure, as well as substantial layoffs in the public sector.<sup>15</sup> As a result, unemployment in Eastern Germany increased further to more than 19 per cent in 1998. With the recovery of the world economy in the late 1990s, the situation also began to improve in Germany. In Western

<sup>15</sup> For a detailed description of the East German process of transition and economic integration see IAB (1998) or Wurzel (2001).

Germany, GDP growth increased from only 0.6 per cent in 1996 to more than 3 per cent in 2000. Unemployment fell from almost 11 per cent in 1997 to about 8 per cent in 2000. In Eastern Germany, on the other hand, the recovery was only short. After stagnation in the period 1997 to 1998, GDP grew by almost two per cent in 1999, but growth already began to decline in 2000. From 2001 to 2003, the East German economy has been shrinking. The unemployment rate remained almost unchanged at about 19 per cent during these years and has reached a new peak of more than 20 per cent in 2003. In Western Germany, economic growth decelerated following the slow down of the world economy after September 11, 2001, and unemployment returned to more than 9 per cent in 2003. Currently, the German economy is suffering from the enormous cost of its high and persistent unemployment and the still to be solved structural problems in Eastern Germany which, supported by a strong Euro which depresses exports, constrain Germany's full participation in the recovery of the world economy. In 2004, the German economy has grown by 1.7 per cent which is the highest rate since 2000. However, the situation on the labour market did not improve. The unemployment rate remained unchanged at about 20 per cent in the East and increased slightly to 9.4 per cent in the West.

Tables 2 and 3 show the structure of registered unemployment in Eastern and Western Germany from 1991 to 2003. There are substantial differences between these two labour markets. Firstly, East German women have been affected by unemployment to a much larger extent than their West German counterparts in the early and mid 1990s. This is the result of a traditionally much higher labour force participation rate of East German women which, in 1991, was 77 per cent compared to only 58 per cent in Western Germany (BA, 2001). However, the participation rates as well as the proportion among the unemployed are converging. In 2003, labour force participation of women was 73 per cent in Eastern Germany compared to 65 per cent in the West, while women made up 49 per cent of the unemployed in the East and 43 per cent in the West (BA, 2004a). There is also a substantial difference with respect to the fraction of non-German unemployed which is much larger in Western Germany. This is due to the fact that the number of non-German nationals living in Eastern Germany is very low though increasing. Another striking difference exists for unemployed individuals without any formal professional degree. While in Eastern Germany these people make up about 20 per cent of the unemployed, the corresponding number for Western Germany is about two times as high. The reason for this is a higher average education level in Eastern Germany which is the result of socialist education policy in the former GDR. With respect to the age structure of unemployment there is a strong convergence in the two parts of Germany. In 2003 the fraction of unemployed individuals below age 25 was 12 per cent while the fraction of elderly people of age 55 or older was almost the same. Individuals with health problems make up between 25 and 30 per cent of the unemployed in Western Germany. The corresponding number

for Eastern Germany has increased over time from about 10 per cent in 1993 to more than 21 per cent in 2003.

**Table 2: Structure of registered unemployment in Eastern Germany 1991-2003**

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Total number	1,029	1,1	1,15	1,04	1,03	1,10	1,37	1,38	1,47	1,44	1,48	1,50	1,554
Thereof (%)													
Women	60.0	64.7	65.4	66.9	63.7	59.6	58.0	54.2	54.2	51.9	50.7	49.1	49.2
Non-German	1.5	1.4	3.2	3.2	3.6	3.7	3.8	4.0	4.3	4.4	4.5	4.8	4.8
No degree	NA	NA	23.2	20.5	21.0	20.8	21.1	24.6	24.4	25.0	24.3	23.4	22.6
Age <25	NA	NA	11.8	11.3	11.0	11.81	11.6	12.4	11.7	13.2	12.9	13.6	12.3
Age ≥55	NA	NA	7.5	12.4	16.4	10.1	19.8	21.4	21.4	15.41	15.4	12.5	10.1
LTU	NA	NA	30.7	34.7	28.8	27.0	29.8	34.6	31.9	35.4	35.3	38.1	43.4
Health	NA	NA	9.9	11.7	13.8	15.7	16.4	18.1	19.4	20.4	21.1	20.8	21.3

Note: The first line states the total number of unemployed individuals in thousand. No degree: no formal professional degree. LTU: at least 12 months (long-term) unemployed. NA: not available. Source: BA (1992b-2004b).

**Table 3: Structure of registered unemployment in Western Germany 1991-2003**

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Total number	1,61	1,78	2,28	2,45	2,48	2,74	2,93	2,58	2,25	2,23	2,25	2,44	2,65
There of (%)													
Women	47.9	46.6	44.04	43.9	44.1	43.5	44.0	45.3	45.8	46.3	45.6	43.9	43.2
Non-German	12.8	14.4	15.3	16.0	16.6	17.3	17.2	17.31	17.0	16.8	17.2	17.2	17.1
No degree	47.3	47.7	46.5	46.3	46.5	46.7	45.7	46.1	45.4	46.2	45.4	42.8	41.3
Age <25	15.2	14.8	12.31	13.3	13.0	12.9	12.4	11.7	11.41	11.4	12.3	12.7	12.2
Age ≥55	19.8	20.5	19.8	21.3	23.0	22.9	22.4	24.3	24.6	23.7	19.4	15.5	11.9
LTU	28.3	26.6	26.0	32.5	32.3	32.7	36.1	37.8	36.8	37.2	32.3	30.0	32.3
Health problems	NA	NA	26.5	26.5	26.3	25.6	25.3	27.1	28.4	29.8	29.2	26.7	25.2

Note: The first line states the total number of unemployed individuals in thousand. No degree: no formal professional degree. LTU: at least 12 months (long-term) unemployed. NA: not available. Source: BA (1992b-2004b).

An interesting pattern can be observed for the proportion of long-term unemployed (LTU). For Western Germany it shows the increasing persistence of unemployment up to 2000. In 2001 and 2002 the rate has declined but started to increase again in 2003. In Eastern Germany the situation was different. Before Unification there was virtually no unemployment. With the dramatic rise in unemployment during the early stages of transition, the proportion of LTU also increased rapidly until 1994. When unemployment dropped in 1995 the fraction of LTU also declined and dropped further in 1996. Since then, however, the proportion of LTU has increased steadily independent of the development of the unemployment rate indicating that East German unemployment has now reached a level of persistence comparable to or even worse than that of Western Germany in 2000.

### 3.1.3. German Labour Market Policy

Until the end of 1997 the legal basis of German Labour Market Policy had been the Employment Promotion Act (*Arbeitsförderungsgesetz*, AFG). Enacted in 1969, it replaced the Job Placement and Unemployment Insurance Act (*Gesetz über Arbeitsvermittlung und Arbeitslosenversicherung*) from 1927 which had become obsolete due to fundamental changes in the economic, social and societal environment. The law had introduced unemployment insurance to the German social security system and its main objective had been to alleviate the negative effects of abrupt loss of labour income when becoming unemployed.

The AFG had been one of the most important sociopolitical laws of the 1960s. Rather than just providing counselling and job placement services as well as passive income support during unemployment, it introduced a variety of new activation measures to German labour market policy. Being established in a situation of almost full employment in Germany their primary objective was to keep employment high and to constantly improve the employment structure in order to foster economic growth (§ 1 AFG). In particular, these measures were aimed at balancing labour demand and supply both quantitatively and qualitatively. Special emphasis was given to training programmes which were designed to constantly adjust and increase the skills of the labour force with the aim of encouraging technological progress and hereby fostering economic growth as well as facilitating fast adjustment of employees' skills to changing demands of employers. § 2 AFG defined the objectives of the policy measures more concretely:

1. to reduce unemployment, underemployment and labour supply shortages,
2. to improve job-related mobility,
3. to eliminate the adverse effects of technological and structural change,
4. to eliminate gender discrimination in the labour market,
5. to improve the labour market integration of disadvantaged people, and
6. to improve the employment structure by region and industry.

In 1981 the goal of reducing illegal employment was added. Although formally these objectives did not change until abolishment of the AFG in 1998, the specific measures provided under the AFG as well as the form and intensity of their use varied substantially over the years depending on the situation in the labour market. Especially after German Unification in 1990 when unemployment rose rapidly and became increasingly persistent, the divergence between the policy instruments provided under the AFG and the needs of the labour market became more and more apparent. Therefore, in 1998, the almost 30 year old and repeatedly amended AFG has been replaced by Social Code III (*Sozialgesetzbuch III*, SGB III) which substantially reformed German labour market policy.

In contrast to the AFG, the measures provided under SGB III focus on jobseekers that are unemployed or directly threatened with unemployment. Against the background of high levels and persistence of unemployment in Germany in the mid 1990s, they are designed with the explicit aim of preventing or reducing unemployment and payment of income support during unemployment (§ 1 SGB III). This is, for example, emphasised by the fact that job placement has been given priority over passive payment of income support during unemployment and all other active measures unless these are necessary for permanent labour market integration (§ 4 SGB III). Under the AFG legislation job placement and all forms of training had had equal priority (§ 5 AFG). Moreover, the new legislation has given local employment agencies more discretion in implementing ALMP. Up to 10 per cent of the ALMP budget can now be allocated to innovative measures that are not defined in the legislation (§ 10 SGB III). One of the most important innovations of SGB III was that a substantial amount of self-responsibility is required from both jobseekers and employers, and also from employees (§ 2 SGB III). Similar to the old regulations, jobseekers have to use every opportunity to find employment and they have to take up any acceptable job, but requirements for independent job search and acceptability of jobs have been tightened.<sup>16</sup> Employers, on the other hand, have to take measures to prevent layoffs and dependence of their employees on the measures provided under SGB III, and they have to announce and fill vacancies as early and as quickly as possible. Employees, with the support of their employers, have to adjust their skills to changing requirements and must not quit an acceptable job without having a new one if they do not want to lose potential benefit claims.

Only a few years after the enactment of SGB III in 1998, the German Federal Government had to realise that the new legislation had not been able to substantially improve the situation in the labour market. The unemployment rate was declining only slightly despite improving economic conditions in the late 1990s and in 2000. Especially in Eastern Germany the situation remained worrying. There, the unemployment rate stayed above 18 per cent and expenditure of the Federal Employment Agency for active and passive labour market policy remained almost unchanged at about e 25 billion. As a consequence, the Federal Government agreed on a complete, stepwise reform of German labour market policy.

As a first step and effective from 2002, the so-called Job-AQTIV<sup>17</sup> legislation has changed the main focus of German labour market policy from an *active* to an *activating* and more preemptive and more flexible labour market policy. The most important innovations of the new legislation are (a) intensification of job search monitoring and placement efforts, in particular, (b) introduction of qualitative profiling to classify jobseekers by their individual strengths, barriers to employment and need for assistance immediately upon registration with the LEA, and (c) written agreement (*Eingliederungsvereinbarung*) between the jobseeker and the local employment agency

<sup>16</sup> The new regulations regarding acceptability of jobs have become effective already in April 1997; see § 103b AFG in the version of March 24, 1997

<sup>17</sup> AQTIV stands for the German equivalents of activate, qualify, train, invest, and place (into jobs).

setting out the placement strategy and the associated obligations of both parties; (d) more preemptive and more flexible use of ALMP, introduction of new ALMP measures and simplification of existing ones; and (e) improvement of the labour market integration of youth and elderly people. In addition, to increase both transparency about how UI funds are spent and the effectiveness of ALMP measures, the Job-AQTIV legislation has introduced the obligation to conduct comprehensive research on the effectiveness of all ALMP measures to SGB III.

The second part of the reform has become known under the synonyms Hartz I, II, III and IV.<sup>18</sup> Effective since 2003, Hartz I and II have provided new foundations for faster and lasting (re)integration of jobseekers into the labour market by opening up new opportunities for temporary work, small jobs, self-employment and employment in private households. In addition, conditions for acceptability of jobs have been tightened further and sanctions in case of non-compliance with conditions for receipt of UI benefits have become stricter but also more flexible. Hartz III, which is effective since 2004, has established the legal foundations for the restructuring of the Federal Employment Agency from a bureaucratic public institution to a modern and efficient service provider as well as a considerable simplification of the policy measures (active and passive) provided under SGB III. Finally, effective since January 2005, Hartz IV has established a common basis for serving all jobseekers without unemployment benefit claims with respect to payment of income support as well as availability of and eligibility for ALMP measures. Following the new principle of 'supporting and demanding' (*Fördern und Fordern*) the main objective of the Hartz IV reform is to increase both employment prospects and work incentives for welfare recipients in order to activate the economic potentials of this group of people and to reduce the number of individuals dependent on social welfare.

### **3.1.4 The Public Employment Service in Germany**

#### **The Federal Employment Agency and its Responsibilities**

In Germany it is the Federal Employment Agency (*Bundesagentur für Arbeit*, BA)<sup>19</sup> which executes the labour market policy for the Federal Government. The BA is a public institution under direct jurisdiction and supervision of the Federal Ministry for Economics and Labour Affairs (*Bundesministerium für Wirtschaft und Arbeit*, BMWA). Affiliated to the BA are 180 local employment agencies (LEAs) with about 660 branch offices which execute the labour market policy for the BA on the regional and local level. In addition, there are ten regional directorates (RDs) which coordinate the activities of the local agencies. The BA gives the overall directions for the

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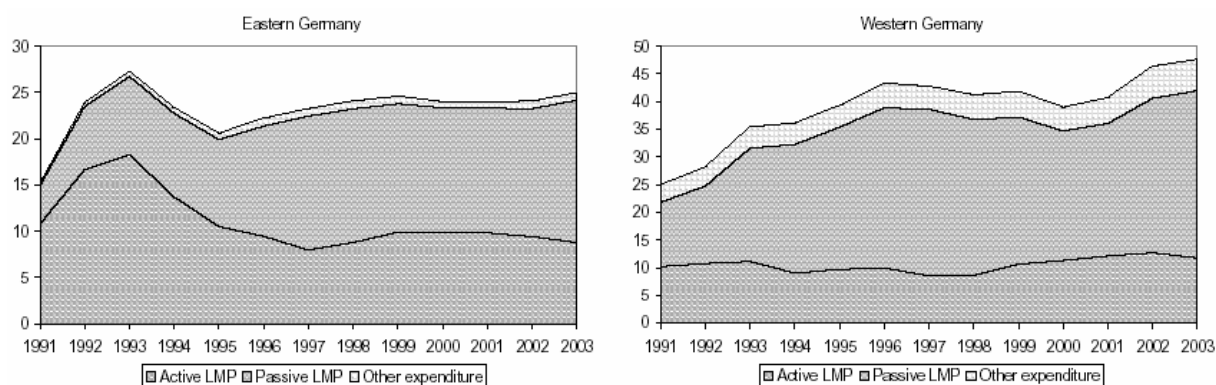
<sup>18</sup> Dr. Peter Hartz had been head of the commission that worked out the proposals for the reform of German labour market policy following the Job-AQTIV legislation. The official names of the four SGB III amendments are: *Erstes, Zweites, Drittes und Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt*

<sup>19</sup> Until the end of 2003: *Bundesanstalt für Arbeit*.

activities of the RDs and LEAs and with this ensures that the labour market policy is executed coherently and consistently in the whole country. The responsibilities of the BA are defined by the duties associated with the provision of the services established by the AFG/SGB III legislation.<sup>20</sup> These can be broadly categorised into counselling and job placement services, labour market training, subsidised employment, support of self-employment, and payment of income support during unemployment. In addition, the BA has to publish detailed labour market statistics on a regular basis. It is also responsible for employment research. While the AFG and earlier versions of SGB III only stated the general obligation to conduct employment research,<sup>21</sup> legislators, with the introduction of the Job-AQTIV legislation, have mandated the BA to conduct comprehensive research on the effectiveness and efficiency of the measures provided under SGB III.<sup>22</sup> The results of this research have to be made available to the public.

The activities of the BA, the RDs and the LEAs are mainly funded by contributions to the unemployment insurance system. In 2003, total UI contributions amounted to e 47 billion and made up about 93.5 per cent of total revenues of the BA. Additional funding is provided by the Federal Government and through financial allocations from third parties.<sup>23</sup> Figure 3 displays the expenditure of the BA from 1991 to 2003 for Eastern and Western Germany. On the one hand, it shows the extensive use of ALMP in Eastern Germany in the first years after Unification. On the other hand, it documents the continuous rise in expenditure for income support during unemployment which is a result of the increasing level and persistence of unemployment in Germany.

**Figure 3: Expenditure of the Federal Employment Agency 1991-2003 in billion euro**



Source: BA (1992a-2004a).

When the German Federal Government started the complete reform of German labour market policy in 2002, it very soon realised that it would also be necessary to reform the more than 30 year

<sup>20</sup> § 3 AFG, §§ 280, 370 SGB III.

<sup>21</sup> § 3 AFG, § 280 SGB III.

<sup>22</sup> § 282 SGB III.

<sup>23</sup> §§ 340, 354-362 SGB III.

old BA in order to fully align goals of the reform and structure of the public employment service. The strongly centralised and bureaucratic institution was no longer compatible with a decentralised, flexible and success-oriented labour market policy. As a consequence, at the beginning of 2004, a complete reform of the BA became effective (Hartz III). In accordance with a success-oriented labour market policy, the former management-by-directives approach has been replaced by a management-by-objectives approach where operationalised goals are set for each LEA taking into account the special circumstances in the local labour market. The RDs, in turn, have the responsibility for the success, i.e. the effectiveness of the regional labour market policy (§ 367 SGB III). The main objectives of the new BA are effective and efficient use of the measures provided by SGB III as well as transparency about how and with which results UI funds are spent. Provision of services has been decentralised and based on the specific, individual needs of the clients of the BA (jobseekers and employers) in order to ensure fulfillment of the set objectives. For this purpose, jobseekers are categorised into different groups according to their individual needs for advice and specific services. Moreover, the change in the overall strategy of the BA has been accompanied by the organisational restructuring of the BA which aims at aligning incentives of BA executives and staff with the new objectives of the BA. In particular, caseworkers are increasingly released from administrative duties to give them more time for their core responsibility of serving clients (jobseekers and also employers), and caseloads are planned to be reduced considerably in the medium run to facilitate more intensive care for each client.<sup>24</sup>

### **Outsourcing of Employment Services**

The Job-AQTIV legislation has been the beginning of a paradigm change in German labour market policy in many respects. One of them is the understanding that efficiency gains may be realised when allowing for more competition in the provision of employment services. Before 2002, competitive elements in the German system had only been of limited relevance. Although the placement monopoly of the BA had been abolished already in 1994, the responsibility for placement of unemployed jobseekers remained almost exclusively with the BA since private placement agencies were focussing on filling vacancies for managers, executives and high-skilled labour on behalf of employers (Konle-Seidl, 2004). Moreover, despite the fact that outsourcing of training and employment programmes to external providers based on contracts with the BA had been common practice, competition was limited since participants were not able to choose their own provider but were assigned directly by the LEA.

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<sup>24</sup> See Knuth (2004) for further details on the organisational restructuring of the BA

In contrast to Australia and the Netherlands which have established systematic contracting-out of all employment services in the course of a complete welfare reform in the late 1990s (see e.g. Bruttel, 2004), Germany has started to build up opportunities for external provision of employment services which are supplementing rather than replacing the previous system. On the one hand, opportunities for private job placement have been extended considerably since 2002. The Job-AQTIV legislation has enabled caseworkers in the LEAs to refer jobseekers to external providers of placement services if this is likely to improve the jobseeker's chances for successful (re)integration into the labour market. Moreover, individuals who have been unemployed for at least six months have a legal claim for referral. The external provider can receive a remuneration for his services from the BA (§§ 37, 37a SGB III). In addition, an explicit competitive element has been introduced. Jobseekers who have not been referred to an external provider by the LEA are - under certain conditions - entitled to financial assistance for private job placement in the form of a so-called placement voucher (*Vermittlungsgutschein*, § 421g SGB III). Eligibility is restricted to UB claimants who have been unemployed for at least six weeks as well as participants in job creation or structural adjustment measures. The validity of the voucher is three months and it entitles the placement agency which has been chosen by the jobseeker to receive a bonus of e 2,000 for placement into insured employment of at least 15 hours per week. However, to prevent abuse, payment of the bonus is performance-based: the first half is paid after six weeks of continuous employment and the rest only after six months.<sup>25</sup>

In addition to increased opportunities for private job placement, new foundations for more competition in the provision of labour market training have been established. Since 2003, participants in further vocational training for whom BA support is granted receive a so-called training voucher (*Bildungsgutschein*) of potentially limited validity with respect to duration, regional area, or specific educational objectives. With this voucher the individual can choose freely among all providers that have been admitted by the BA (§§ 77, 84-86 SGB III). The idea underlying both training and placement vouchers is that jobseekers will only choose good providers with high success rates so that providers are encouraged to improve the quality of their services and, in the longer run, only good providers will survive. However, critics of these vouchers argue that jobseekers - in contrast to the LEAs - do not have enough information to be able to correctly distinguish good from bad providers (Konle-Seidl, 2004).

As another part of the reform, competitive contracting-out of reintegration services for specific target groups has been enabled for the period 2003 to 2005 (§ 421i SGB III). The main objective of this instrument is to test alternative concepts for the (re)integration of jobseekers into the

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<sup>25</sup> Before 2005 the requirements that had to be fulfilled for the placement agency to receive the amount certified in the voucher had been less restrictive. Yet, during the first two trial years of placement vouchers a considerable number of cases of abuse had been discovered so that requirements have become much stricter in 2005.

labour market, but it is also a test of how well competitive contracting-out of employment services works in Germany. External providers can make independent proposals for innovative measures specifically designed for enabling the labour market integration of the target group that has been put to tender by the BA (e.g. long-term unemployed, youth below age 25, elderly people above age 50). The BA then decides which proposal to accept based on both the quality - i.e. the chances for reaching the objectives set by the BA - and the price of the concept. Remuneration of the providers that have been selected by the BA is performance-based in order to provide incentives for both effective and efficient provision of employment services.

Another instrument closely related to the idea of outsourcing of employment services is BA supported temp-work which has been introduced in 2003 (§ 37c SGB III). Based on an agreement between a temp-work agency (TWA) and the LEA, the TWA can employ jobseekers proposed by the LEA to let them work for employers temporarily in need of workers. From the point of view of the BA the hope is that these temporary employments work as a bridge to permanent placement into a job with one of these employers. And even if this is not the case, it still provides work experience and helps to maintain attachment to the labour market. BA support is usually

limited to nine months and remuneration includes both a monthly flat-rate payment which is decreasing over time, and a performance-related bonus in case of successful placement of the jobseeker into a job. In times in which the jobseeker does not work for another employer during the term of the contract, the TWA is obliged to assist him in searching for a permanent job and to provide opportunities for further qualification. Similar to measures according to § 421i SGB III, the BA contracts out these services to applying TWAs (Konle-Seidl, 2004).

### 3.1.5 The Unemployment Insurance System

Unemployment insurance (UI) has been established in 1927 of the German social insurance system after health insurance, accident insurance and pension insurance.<sup>26</sup> UI funds are used not only for payment of income support during unemployment but also for the provision of employment services. UI is compulsory for all employees with more than a minor employment including apprentices in vocational training. However, civil servants (*Beamte*), judges, professional soldiers, clergymen and some other groups of persons are exempted from contributions.<sup>27</sup> Self-employed individuals are not covered by German UI.<sup>28</sup> The total UI contribution is shared equally between employer and employee. Before German Unification in 1990, the contribution had been 4.3

<sup>26</sup> In 1995, compulsory long-term care insurance has been added as the fifth pillar.

<sup>27</sup> §§ 168-169c AFG, §§ 24-28 SGB III. Minor employments are jobs with a salary less than e 325 (e 400 since April 2003) as well as short-term and occasional jobs.

<sup>28</sup> However, from February 2006 on individuals that start their own business can apply for voluntary UI if they had been subject to UI contributions for a certain period of time in the past. See § 1 No. 20 Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt.

per cent of the employee's gross salary.<sup>29</sup> In order to be able to cover the cost of the dramatic increase in unemployment in Eastern Germany after Unification,<sup>30</sup> the contribution was raised temporarily to 6.8 per cent for 1991 but was then reduced to 6.3 per cent for the next two years. Since 1994 the contribution is stable at 6.5 per cent. For some groups of people who are subject to UI contributions but do not receive regular salaries the contribution is paid by the Federal Government or some other institution. These include individuals in rehabilitation measures, people who receive sickness benefits, women on maternity leave, and prisoners.

### Unemployment Benefits

Persons who have contributed sufficiently to the UI can receive unemployment benefits (*Arbeitslosengeld*, UB) for a limited period of time in case of unemployment. A legal entitlement to UB can be acquired if the jobseeker has contributed to the UI for at least twelve months within an entitlement qualification period of three years before the beginning of the unemployment spell. For seasonally employed individuals the minimum contribution period is reduced to six months.<sup>31</sup> After exhaustion of UB, a new claim can be acquired if sufficient months of contributory employment have been accumulated in the meantime. Since 1994, UB claimants receive 67 per cent of their previous average net earnings from insured employment if they have at least one dependent child, and 60 per cent without children.<sup>32</sup> Before, the replacement rates had been 68 per cent and 63 per cent, respectively. UB recipients can earn additional labour income without losing their UB claim if they work less than 15 hours per week. But, except for a small allowance of 20 per cent of the UB payment or at least e 165, it will reduce the benefit payment accordingly.<sup>33</sup>

**Table 4: Maximum duration of unemployment benefit entitlement**

Year	Age	Cont	ME	Age	Cont	ME	Age	Con	ME	Age	Cont	ME	Age	Cont	ME
1990-1996	≤41	24	10	≥42	36	16	≥44	44	19	≥49	52	23	≥54	64	28
1997	≤44	24	10	≥45	36	16	≥47	44	19	≥52	52	23	≥57	64	28
1998-2005	≤44	24	12	≥45	36	18	≥47	44	22	≥52	52	26	≥57	64	32
2006-	≤54	24	12	≥55	36	18	-	-	-	-	-	-	-	-	-

Note: Age in years, contribution period (Cont.) and corresponding maximum duration of entitlement (ME) in months.

The minimum duration of UB entitlement is six months. The maximum duration increases stepwise with the total duration of insured employment within an extended entitlement qualifi-

<sup>29</sup> Up to the upper earnings limit for social insurance contributions. In 2004 the limit was e 61,800 per year for Western Germany and e 52,200 per year for Eastern Germany.

<sup>30</sup> The former German Democratic Republic did not have unemployment insurance. Special regulations in the Unification Treaty, however, ensured eligibility for unemployment benefits and most ALMP measures of essentially every East German becoming unemployed during the years directly after Unification.

<sup>31</sup> § 104 AFG, §§ 123-124 SGB III.

<sup>32</sup> § 111 AFG, § 129 SGB III.

<sup>33</sup> § 115 AFG, § 141 SGB III.

cation period of seven years, and age.<sup>34</sup> Table 4 lists the maximum duration of UB entitlement (*ME*) with the corresponding age limits (*Age*) and minimum contribution periods (*Cont.*) for the years since German Unification. In 1997 UB entitlement had been reduced for the age group 42-56 by raising all age limits by three years. With the introduction of SGB III in 1998, UB entitlement has increased for all age groups. Yet, as one part of the complete reform of the German UI system and becoming effective in February 2006, UB entitlement will be made considerably less generous in order to lower the cost of unemployment directly and to reduce moral hazard in the UI by stimulating job search efforts of UB recipients. The minimum contribution period will be twelve months for all employees including seasonal workers and the entitlement qualification period will be reduced to two years. In addition, the extended entitlement qualification period will be shortened from seven to only three years and the maximum duration of UB entitlement will be reduced substantially for the age group above 44.<sup>35</sup>

In addition to previous contribution and age, participation in ALMP measures can have direct implications for the duration of UB entitlement as well. On the one hand, wages received during participation in employment programmes had been subject to UI contributions until 2003 and had therefore counted in the same way as regular non-subsidised employment for the accumulation of UB claims. On the other hand, receipt of income support during BA supported training (so-called maintenance allowance, MA) affects UB entitlement. Under the AFG legislation, times of receipt of MA had counted in the same way as insured employment, thus contributing to the accumulation of UB claims.<sup>36</sup> After introduction of SGB III, months in receipt of MA were no longer counted as equivalent to months of contributory employment; they now only extended the entitlement qualification period by up to two years (§ 124 SGB III). Since 2003, however, receipt of MA reduces the total duration of UB entitlement by half of the duration of the programme and, since 2004, it no longer extends the entitlement qualification period. Overall, the 2004 reform has almost eliminated incentives to participate in employment or training programmes for the sole purpose of accumulating UB claims.

To be able to claim UB, jobseekers must register as unemployed at the LEA.<sup>37</sup> A caseworker then conducts an initial interview with the jobseeker to check eligibility for UB, to inform him about the services provided by the LEA, and to outline the obligations associated with receipt of benefits. The latter include independent job search, availability for job placement, take-up of any job that is acceptable, as well as willingness to participate in all activation measures proposed by the case-

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<sup>34</sup> § 106 AFG, § 127 SGB III.

<sup>35</sup> §§ 124, 127, 434j SGB III in the version of January 1, 2004.

<sup>36</sup> § 107 AFG in conjunction with § 104 AFG.

<sup>37</sup> Since July 2003 jobseekers are obliged to register as searching for a job with the LEA right after notification of their dismissal in order to facilitate quick placement into a new job (§ 37b SGB III).

worker.<sup>38</sup> Since introduction of the Job-AQTIV legislation in 2002, qualitative profiling which assesses individual strengths and barriers to employment is used to classify jobseekers into job-ready, counselling and intensive service clients immediately upon registration with the LEA (Mosley, 2005).<sup>39</sup> Based on this assessment a placement strategy is developed and written down in a so-called jobseeker's agreement (*Eingliederungsvereinbarung*) which is signed by the caseworker and the jobseeker. It sets out both the services provided by the LEA, and the obligations of the jobseeker regarding independent job search and participation in activation measures (§§ 6, 35 SGB III).

After the initial interview, the caseworker can schedule a meeting at any time to check compliance with benefit conditions, i.e. the jobseeker's agreement, or to discuss new job offers available, potential benefits of participating in labour market programmes, or adjustment of their job placement strategy. Attendance is compulsory for UB claimants.<sup>40</sup> In case of non-compliance with benefit conditions, the UB payment can be suspended for up to twelve weeks. The total UB claim is reduced accordingly. Repeated offences accumulating to a total sanction period of 24 weeks cease the UB entitlement completely.<sup>41</sup> With the Job-AQTIV legislation and Hartz I, job search monitoring has been intensified and benefit sanctions have become stricter but also more flexible. For example on the one hand, Hartz I has shifted the burden of proof from the LEA to the jobseeker. On the other hand, sanction periods are now different for different kinds of offences (§ 144 SGB III). Also, in contrast to the past, they are more rigorously enforced. As a result, the number of sanctions that actually have been imposed has almost tripled from 57,000 in 2002 to 153,000 in 2003 (BMWA, 2004).

### **Other Forms of Income Support during Unemployment**

Until the end of 2004, German social insurance had discriminated between former recipients of UB and people who had not contributed sufficiently to the UI.<sup>42</sup> Unemployed individuals who had exhausted their UB claim could receive unemployment assistance (*Arbeitslosenhilfe*, UA). Like UB, UA was proportional to previous earnings but with lower replacement rates than UB (57 per cent with and 53 per cent without dependent children). Also, benefit conditions and sanctions regarding registration, independent job search, take up and acceptability of employment as well as participation in activation measures had been essentially the same as for UB. In contrast, people who had never been eligible for UB could only qualify for social assistance (*Sozialhilfe*, SocA) which was a monthly flat-rate payment unrelated to previous earnings and, in general, considerably

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<sup>38</sup> §§ 100-103 AFG, §§ 117-119 SGB III.

<sup>39</sup> See also Adema, Gray and Kahl (2003) for further details.

<sup>40</sup> § 132 AFG, § 309 SGB III. From 1994 to 1997 a meeting had to be scheduled at least every three months.

<sup>41</sup> § 119-119a AFG in conjunction with § 103 AFG, § 144 SGB III.

<sup>42</sup> Similar systems are still existing in several OECD countries, e.g. in Austria, France and the Netherlands.

lower than UA.<sup>43</sup> Both UA and SocA had been means tested and paid from tax revenue. Also, the duration of the UA/SocA claim had been potentially unlimited. As long as the individual had satisfied all benefit conditions, UA/SocA had been paid until reaching retirement age. Like UB, UA had been administered by the BA though funding had come from the Federal Government and not the UI, while SocA had been administered by the local authorities (municipalities and counties). Besides the amount of benefits, the most important difference between recipients of UA and SocA had concerned eligibility for ALMP measures. While the ALMP measures provided by the AFG/SGB III legislation had been open to UA claimants, recipients of SocA had had access only in exceptional cases.

With the Hartz IV reform, one of the most important parts of the reform of German social policy has become effective on January 1, 2005. Both UA and SocA have been abolished. Instead, a common financial basis has been established for all individuals who cannot provide for themselves and do not receive income support from any other social security institution. In

this respect, Germany is converging to the majority of OECD countries. The legal basis for the new regulations is Social Code II (*Sozialgesetzbuch II*, SGB II). Needy individuals who are capable of working but do not qualify for regular UB receive so-called unemployment benefits II (*Arbeitslosengeld II*, UB II) as well as additional allowances for accommodation and heating costs. Their dependants who are living in the same household and who are not capable of working receive so-called social benefits (*Sozialgeld*) which are somewhat lower than UB II. Similar to former social assistance, both forms of benefits are means tested and paid monthly at flat rates which are independent of previous earnings and UI contribution.<sup>44</sup>

The most important objective of the Hartz IV reform is to reduce the number of welfare dependent individuals by reintegrating those capable of working into the labour market independent of their UI status. For this purpose, the LEAs together with the local authorities which had administered SocA, have set up new so-called *Job-Centers* which provide employment services to all jobseekers as one-stop centers (§ 9 SGB III).<sup>45</sup> In this respect, Germany is following the example of the United Kingdom, the United States and Australia which have established one-stop centers already several years ago. Provision of services is based on individual need for assistance and independent of the form of benefit being received. In particular, individuals who have not contributed sufficiently to the UI are no longer excluded from the instruments of ALMP provided by SGB III. Moreover, SGB II has introduced additional measures which have been designed specifically for welfare recipients and their particular barriers to employment like e.g. debt, abuse of alcohol or

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<sup>43</sup> In cases where UA had been lower than the regular SocA rate, UA had been supplemented by SocA.

<sup>44</sup> §§ 19-28 SGB II. For individuals who have exhausted their regular UB claim, the UB II payment is higher than the regular rate for the first two years of receipt of UB II.

<sup>45</sup> As an experiment, the German Federal Government has also admitted 69 local authorities to opt for exclusive provision of employment services to recipients of UB II or social benefits. See Box 2 and §§ 6a-c SGB II.

other drugs, etc. (§ 16 SGB II). Within the Job-Centers, the LEAs are responsible for all activation measures (SGB II and III) as well as payment of UB II and social benefits. Funding for these services is provided out of the federal budget. The local authorities, on the other hand, are responsible for reimbursement of accommodation, heating and one-time costs for e.g. initial furnishing and clothes, child care services, as well as debt, socio-psychological and drug counselling (§ 6 SGB II).

The LEA assigns each welfare dependent individual capable of working a caseworker who should be responsible for no more than 75 clients.<sup>46</sup> In accordance with the new principle of 'supporting and demanding' (*Fördern und Fordern*) and similar to UB claimants, the jobseeker and his caseworker sign a jobseeker's agreement (*Eingliederungsvereinbarung*) which has a duration of six months and states both the services that will be provided to the jobseeker, and his obligations regarding independent job search and participation in employment, training or other ALMP programmes (§ 15 SGB II). Recipients of UB II or social benefits have to take all measures to end their dependence on social welfare. In particular, they have to take any acceptable job or work opportunity that is offered to them, and they must participate actively in any measure proposed by the caseworker to improve their chances for successful labour market integration (§ 2 SGB II). In this respect, benefit conditions are very similar to those for regular UB. In case of non-compliance with benefit conditions, benefits will be cut by 10 to more than 30 percent. To encourage recipients of UB II or social benefits to take up employment, work incentives have been extended considerably compared to both UA and SocA. In the past, people had almost no incentive to take up a low-paid or part-time job because the additional income earned would reduce their benefits by the same amount (except for a small allowable deduction) so that they could hardly improve their economic situation by working. On the one hand, recipients of UB II can receive a monthly bonus (so-called *Einstiegs geld*) for up to 24 months when taking up insured employment or becoming self-employed (§ 29 SGB II). On the other hand, up to monthly gross earnings of euro 1,500 only part of additional income earned is deducted from the benefit payment (§ 30 SGB II).

### **3.1.6 Active Labour Market Policy**

#### **The Instruments of German ALMP**

Active labour market policy has a long tradition in Germany and among OECD countries, expenditure on ALMP is one of the highest (see Figure 2). The first ALMP measures have been established by the AFG already in 1969, and some of them are still used today. However, their specific design and the intensity of their use changed considerably over the years depending on the

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<sup>46</sup> At the moment, this target can only be fulfilled for youth below age 25. Before the restructuring of the BA in 2004, caseworkers had been responsible for up to 800 clients so that it will take some time until the target of 75 clients can be reached (Winkler, 2004).

situation in the labour market. With the dramatic rise in unemployment after German Unification in 1990, ALMP has become one of the most important economic policy instruments of the German Federal Government. In contrast to passive payment of income support during unemployment, ALMP measures aim at improving individual labour market outcomes by increasing the employability of the individual, e.g. through training, and by improving individual access to the labour market (OECD, 1993). The instruments traditionally used in German ALMP can be categorised into counselling and job placement services, labour market training, subsidised employment, support of self-employment, and other measures.

### **Counselling and Job Placement Services**

The LEAs provide extensive counselling and job placement services to all individuals searching for a job or an apprenticeship. These include provision of information and advice regarding career options and employment prospects, the situation in the labour market, job and apprenticeship vacancies, as well as the availability of ALMP measures. One way of providing these services is through an extensive electronic information system that is accessible from both inside and outside the LEAs. In the LEAs, jobseekers have access to computers that can be used for the search for vacancies in both the BA databases and the internet, for accessing other information systems of the BA, as well as for writing applications. Until 1994 there had existed a placement monopoly of the BA. Other institutions could conduct job placement only in exceptional cases by order of the BA. In 1994 private placement services have been permitted but until 2002 a license from the BA was needed. In the course of the reform of German labour market policy since 2002, opportunities for private job placement have been extended considerably. Moreover, with the aim of achievement of an improved image and a higher market share of notified vacancies, placement services for employers have also improved. Besides an improved data base on job openings and better controlling data on the matching process, the LEAs have established integrated service teams which seek and maintain contact with key employers in the region.

### **Labour Market Training**

Training has always been one of the most important measures of German ALMP. Germany belongs to the OECD countries with the highest expenditure on labour market training measured as a percentage of GDP after Denmark and the Netherlands, and it makes up the largest fraction of total expenditure on ALMP. The BA supports labour market training by providing income support during participation and by bearing the direct cost of the programme such as course fees and study material, as well as additional expenses for child care, transportation and accommodation. The training programmes differ largely in their human capital augmenting nature. Five groups of programmes can be distinguished: (i) short training, (ii) basic vocational training, (iii) further vocational training, (iv) retraining, and (v) German language courses. During the

first years after enactment of the AFG in 1969 when unemployment was low, BA supported training was used to constantly increase the skills of the labour force with the aim of fostering economic growth as well as facilitating fast adjustment of employees' skills to changing requirements of employers. With rising unemployment after the oil price shocks in the 1970s the focus shifted towards measures aimed at eliminating skill deficits of unemployed individuals. This was particularly the case in Eastern Germany directly after Unification. With the rapid transformation from a centrally planned to a market economy the East German labour force faced a completely changed demand for skills in the labour market. As a consequence, training became one of the most important ALMP instruments during East German transition.

### 3.1.7 Subsidised Employment

Subsidised employment is an important instrument of ALMP in many OECD countries. In Germany, contrarily to e.g. Belgium, Ireland and Spain, this measure is less important than labour market training in terms of expenditure. There exist two forms of subsidised employment in Germany: temporary wage subsidies and employment programmes.

*Temporary wage subsidies* can be either direct or indirect. Most *direct* temporary wage subsidies aim at reintegrating unemployed individuals with reduced productivity by providing incentives for firms to employ these jobseekers. The wage subsidy compensates employers for the reduced work capacity during the first months in a new job. The target group for this measure are persons with barriers to employment like e.g. long-term unemployed individuals, elderly people and disabled persons. Usually, the subsidy is paid during the first six months in the new job, in exceptional cases extensions to a total of up to twelve months are possible. This instrument has existed under different labels and varying but similar designs in Germany.<sup>47</sup> Another form of direct temporary wage subsidy exists since 2002 and has become known under the label of *job rotation*. It is, in fact, a hybrid between support of further vocational training and subsidised temporary employment of unemployed individuals. Employers who send an employee to a full-time training course can receive a wage subsidy from the BA if they employ an unemployed person as replacement for the duration of the course. The subsidy compensates for both the employer's cost of the training course, and the potentially reduced work capacity of the replacement worker.

*Indirect* temporary wage subsidies, on the other hand, are paid to employees. Short-time work (*Kurzarbeit*, STW) compensations aim to prevent layoffs due to temporary, unanticipated reductions in a firm's labour demand. Employees in STW work significantly less than their contractually agreed working hours. They receive income support from the BA to supplement their reduced

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<sup>47</sup> Einarbeitungszuschuss (§ 49 AFG), Eingliederungsbeihilfe (§ 54 AFG). Eingliederungszuschuss (§§ 218-224 SGB III), Einstellungszuschuss bei Neugründung (§§ 225-228 SGB III), Eingliederungsvertrag (§§ 54a-c AFG, §§ 229-234 SGB III) which has been abolished in 2002.

labour income. STW was extensively used in Eastern Germany in the first years after Unification. There, until 1992, STW compensations were also paid if the working hours were reduced to zero and even if it was clear that the reduction in labour demand was permanent. Another form of indirect wage subsidies has been designed specifically for workers in the construction industry. Construction workers who cannot be laid off temporarily due to dismissal protection regulations are compensated for income losses due to seasonal or weather-related lack of work. The last form of indirect wage subsidy had existed from 1996 to 2004. The so-called employee assistance (*Arbeitnehmerhilfe*) had been designed to encourage UA recipients to take up temporary employment in the regular labour market in order to maintain their employability and their attachment to the labour market. Eligible individuals had been granted income support during regular but temporary employment of no more than three months.<sup>48</sup> From 1998 to 2002 this measure had also been available to recipients of UB (§ 421b SGB III).

In times of high and persistent unemployment *employment programmes* are an important measure to maintain the employability of unemployed and especially long-term unemployed individuals, as well as to preserve social stability in regions with particularly high rates of unemployment. Usually, a variety of non-market jobs that are in the interest of the public is provided. The oldest form of employment programmes in Germany are so-called job creation schemes (*Arbeitsbeschaffungsmassnahmen*, ABM). Until 2003, the BA supported providers of ABM by subsidising between 30 and 100 per cent of the salaries of ABM-employees.<sup>49</sup> The specific rate depended on the situation in the local labour market as well as the jobseeker's 'need' for support as measured by the severeness of his barriers to employment. Normally, the maximum duration of ABM was one year but it could be extended to a total of up to three years in exceptional cases. Until 2001, eligibility was limited to jobseekers with an unemployment record of at least six months within the year prior to assignment to ABM.<sup>50</sup> The Job-AQTIV legislation abolished this requirement. In accordance with the new objectives of German labour market policy, LEA staff should be able to use ABM early in the unemployment spell if this seemed appropriate to increase the jobseeker's chances for finding a job.

In order to facilitate creation of new jobs in economically weak regions and to compensate substantial layoffs which have strong adverse impacts on the local labour market, so-called structural adjustment measures (*Strukturanpassungsmassnahmen*, SAM) have been introduced with

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<sup>48</sup> § 134b AFG, § 56 SGB III.

<sup>49</sup> Since 2002 the BA also had the possibility to pay a fixed monthly subsidy that is differentiated by education level (§ 265a SGB III).

<sup>50</sup> §§ 91-99 AFG, § 9 Anordnung des Verwaltungsrates der Bundesanstalt für Arbeit über die Förderung von allgemeinen Massnahmen zur Arbeitsbeschaffung aus Mitteln der Bundesanstalt, §§ 260-271 SGB III. Until 1997, there had also existed a special form of ABM for unemployed individuals above age 50 with less restrictive eligibility criteria and longer durations (§ 97 AFG).

SGB III in 1998.<sup>51</sup> In contrast to ABM, SAM are targeted at individuals with particularly bad employment prospects, and they are much more restricted with respect to the kind of jobs that can be supported. SAM providers receive a fixed monthly subsidy for each participant. The duration of SAM is normally no longer than three years but it can be extended to a total of up to four years. Since 2002 durations of up to five years are possible for individuals of age 55 and older.<sup>52</sup> Since 2002, the BA also subsidises so-called job creating infrastructure measures (*Beschäftigung schaffende Infrastrukturmassnahmen*, BSI). The objective of this instrument is to support projects that improve the local infrastructure and create new jobs in the regular labour market. In order to ensure creation of additional jobs, the number of employees assigned by the LEA must not exceed 35 per cent of all BSI employees and the total subsidy should not exceed 25 per cent of the total cost of the project (§ 279a SGB III).

In the course of the reform of German labour market policy, employment programmes have been reformed completely as well in 2004. Under the label of ABM, SAM and ABM have been integrated into one, considerably simplified instrument. BSI, on the other hand, have been extended to measures that improve the environment. The new ABM aim at improving the employability of unemployed individuals in regions with high unemployment. Providers receive a fixed monthly subsidy for each employee which is differentiated by education level of the participant. The maximum duration of the new ABM is two years for employees below age 55, and three years otherwise. Another important innovation has been the exemption of employment in ABM from social insurance contributions (§27 SGB III). In the past, participation in ABM had counted as contributory employment for UB entitlement. From the point of view of the BA, the new legislation makes support of ABM much more incentive compatible since it prevents abuse of ABM for the sole purpose of accumulating UB claims.

### 3.1.8 Support of Self-Employment

In Germany, there exist different instruments to encourage unemployed individuals to start their own enterprise and become self-employed. Firstly, so-called bridging allowances (*Überbrückungsgeld*) can be granted by the BA to formerly unemployed individuals for the first six months while starting their own enterprise. The allowance is composed of an amount equal to the UB or UA payment the individual has or would have received during unemployment and a fixed payment for social insurance contributions. Since 2004, individuals who end or prevent their unemployment by becoming self-employed have a legal claim for bridging allowances.<sup>53</sup> Secondly, since 1997, owners of an enterprise not older than two years with no more than five employees can receive a wage

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<sup>51</sup> In fact, SAM replaced two other forms of employment programmes introduced specifically for Eastern Germany in 1993 (so-called *Produktiver Lohnkostenzuschuss Ost*, § 249h AFG) and for Western Germany in 1994 (so-called *Produktive Arbeitsförderung*, § 249s AFG).

<sup>52</sup> §§ 272-279 SGB III.

<sup>53</sup> § 55a AFG, § 57 SGB III.

subsidy from the BA when employing a jobseeker who has been unemployed or in some ALMP measure for at least three months and who could not find a job otherwise. The BA subsidises 50 per cent of the salary of the newly employed for up to twelve months.<sup>54</sup> Finally, in 2003 another instrument to encourage self-employment has been introduced which is complementary to bridging allowances. Recipients of income support during unemployment and participants in ABM or SAM that end their unemployment by starting their own small enterprise with expected yearly earnings of no more than e 25,000 have a legal claim for a fixed monthly payment from the BA (*Existenzgründungszuschuss*, ExGZ). The support can be granted for up to three years but decreases each year.<sup>55</sup> In contrast to bridging allowances, ExGZ recipients are subject to public pension insurance contributions. Self-employment of formerly unemployed is also supported in several other OECD countries, e.g. in Denmark, the Netherlands, Sweden and Switzerland.

### 3.1.9 Other ALMP Measures

In addition to the instruments discussed above, there exist several other ALMP measures with very specific objectives. On the one hand, there are supplementary instruments that are designed to encourage unemployed individuals to take up employment by reducing the costs associated with job search and take-up of a new job, and by increasing mobility.<sup>56</sup> The BA provides financial assistance for covering transportation or moving expenses, as well as expenses for special equipment (e.g. special clothes) needed in the new job. In addition, the BA provides grants to bridge the time between take-up of the new job and the first salary payment. Until 1997 the BA had also reimbursed part of the application cost during job search.<sup>57</sup>

On the other hand, there are measures specifically targeted at certain groups of people. These exist in addition to special - usually less restrictive or more generous - regulations for the standard measures discussed above that are applied to persons with special barriers to employment like e.g. long-term unemployed individuals, youth, elderly people and the disabled. One instrument targeted the long-term unemployed had been so-called *Beschäftigungshilfen für Langzeitarbeitslose* which had existed from 1989 to 2002. It was a direct wage subsidy paid by the BA to firms which employed jobseekers who had been unemployed for at least one year. Depending on the duration of previous unemployment, between 40 and 80 per cent of the employee's salary were subsidised. Moreover, in the period 2003 to 2004, the German Federal Government supported another 100,000 individuals above age 25 who had been unemployed for more than six months by paying a monthly

<sup>54</sup> So-called *Einstellungszuschuss bei Neugründung*, see § 55b AFG, §§ 225-228 SGB III.

<sup>55</sup> The payment amounts to e 600, 360 and 240 for year 1, 2 and 3, respectively; see § 4211 SGB III. Until the end of 2003, support was restricted to one-person or pure family businesses (so-called *Ich-AG* or *Familien-AG*).

<sup>56</sup> Another group of supplementary ALMP measures are programmes that are supported with funds from the European Social Fund (ESF). These are targeted at individuals usually not eligible for BA support and include vocational training, training while receiving STW compensations, and support of self-employment.

<sup>57</sup> § 53 AFG, §§ 53-55 SGB III. Since 2003 these services are also provided to individuals threatened with unemployment which take up a new job. This had also been the case under the AFG legislation.

case-based compensation for the provision of work opportunities by the municipalities. This programme has been replaced by the measures provided under the new SGB II legislation at the beginning of 2005.

In the period 1999 to 2004, the German Federal Government had also launched several programmes providing both specific measures and additional funding for integrating youth below age 25 into the labour market. The main objectives of these programmes had been extension of the supply of apprenticeships, provision of training and work opportunities for youth who have not found an apprenticeship as well as a significant reduction in the caseload of the caseworkers in the LEAs. Total expenditure on youth measures amounted to 0.1 per cent of German GDP in 2002.

For elderly individuals there exist early retirement schemes which seek to lower unemployment directly by reducing the labour supply of elderly individuals. Besides the traditional early retirement pensions which are not directly targeted at unemployed individuals, eligibility requirements for UB with respect to job search, acceptance of job offers and participation in ALMP measures are eased for individuals that are 58 or older.<sup>58</sup> Also, in response to the dramatic decline in labour demand in Eastern Germany in the early 1990s, § 249e AFG (later § 429 SGB III) had been enacted for individuals living in Eastern Germany who had become unemployed at the age of 55 or older between October 3, 1990 and December 31, 1991 and who qualified for the maximum duration of UB entitlement. To reduce labour supply, this regulation released these individuals from the obligation to search for a job while receiving benefits from the BA. Instead of UB they received so-called pension transition allowances (*Altersübergangsgeld*). Today, total expenditure on early retirement is relatively low compared to other OECD countries like Denmark, Finland or Belgium.

There are also measures specifically targeted at the disabled and other individuals with health problems. The services provided to this special group include all measures that are also available to other individuals but the eligibility requirements are less restrictive. In particular, individuals need not necessarily be unemployed in order to be eligible for ALMP measures. The BA also bears the additional costs arising from the disability or health problem. The objective of these measures is to maintain and improve the employability of this group of persons and to ensure their integration into the labour market.<sup>59</sup> Total expenditure is substantial compared to other OECD countries, and almost as high as for labour market training.

### **3.1.10 Use of ALMP Measures in Germany**

Figure 5 shows the expenditure for ALMP in Eastern and Western Germany for the years 1991 to 2003. Since 1991, the BA has spent between 35 and 67 per cent of its annual budget on

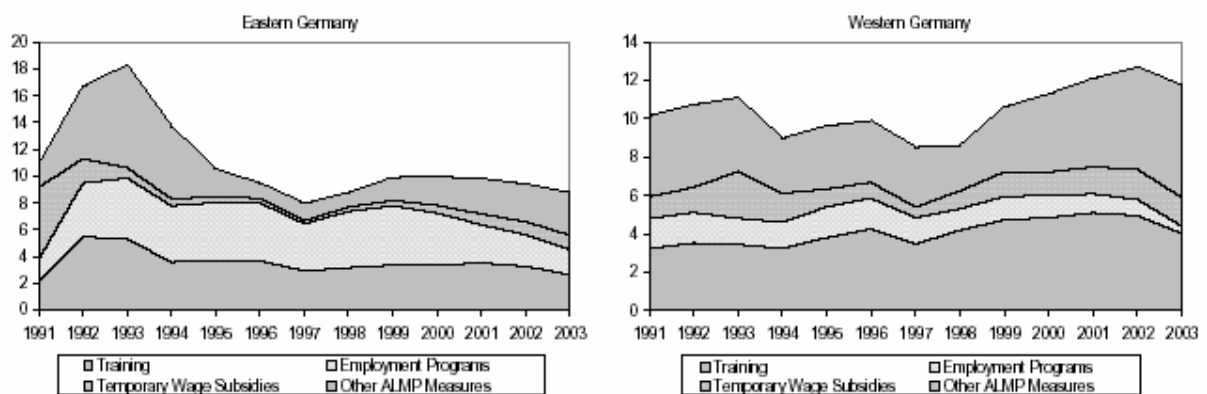
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<sup>58</sup> § 150c AFG, § 428 SGB III.

<sup>59</sup> §§ 56-62 AFG, §§ 97-115 SGB III

ALMP with a disproportionately high share going to Eastern Germany which only makes up about one sixth of the German labour force. The dramatic developments in Eastern Germany in the early 1990s required a very specific use of ALMP measures. On the one hand, the East German economy was contracting rapidly leading to substantial reductions in labour demand. To cope with the immediate strongly adverse effects of this, short-time work and early retirement schemes were used extensively. On the other hand, the skills of the labour force did not meet the requirements of a modern market economy, so that different kinds of training programmes were used on a large scale in order to eliminate these skill deficits. As unemployment kept rising and became very persistent, employment programs also became one of the most important ALMP measures.

**Figure 4: Expenditure on ALMP 1991-2003 in billion euro**



Source: BA (1992a-2004a).

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In 1991, almost half of East German ALMP expenditure was devoted to short-time work (STW). In order to instantaneously reduce the tension in the labour market due to the rapid and dramatic decline in labour demand in that year, more than 1.6 million people were directly absorbed into STW. The main objective of STW in that year was to delay the transition into unemployment in order to prevent the official unemployment rate from skyrocketing. Another 0.8 million individuals were referred to labour market training (FVT). Among them, 25 per cent participated in short training according to §41a AFG. In addition, 0.2 million individuals were assigned to job creation schemes (ABM). In 1992, the number of recipients of STW compensations declined considerably while use of ABM and training was extended significantly. Also, substantial expenditure was devoted towards payment of pension transition allowances (included in 'Other ALMP Measures' in Figure 4) in the period 1992 to 1994.

In 1993, the pattern of ALMP provision in Eastern Germany began to stabilise. Due to abolishment of short training according to § 41a AFG, inflows into training declined sharply to less than 0.3 million. Since then, the number has decreased further with substantial reductions in

1997 and 2003. In these two years, ALMP expenditure had been cut significantly. Since 1998, FVT and retraining are increasingly replaced by short training (training measures; TM) which are much shorter (one month on average) and therefore less costly than FVT and retraining. TM inflows have increased from 167,000 in 1999 to 376,000 in 2003. Corresponding to their share among the unemployed, women have always made up a substantial part of training participants in Eastern Germany (42-66 per cent). The same is true for long-term unemployed individuals (25-33 per cent). In accordance with the objectives of labour market training, another important group of participants are individuals without any professional degree. The fact that their proportion (11-16 per cent) is much smaller than in Western Germany (31-41 per cent), just reflects the difference in the structure of unemployment in the two parts of Germany (see Tables 2 and 3). The proportion of young people below age 25 has increased over time from 9 per cent in 1995 to 21 per cent in 2003.

While STW lost its importance after 1993, employment programmes (ABM and later SAM) remained an important instrument of ALMP in Eastern Germany even though the number of participants declined from 237,000 in 1993 to 110,000 in 2003. ABM have been used extensively for long-term unemployed individuals (60-89 per cent) and individuals above age 50 (32-47 per cent). For SAM, the share of long-term unemployed individuals has always been lower but also substantial (30-53 per cent). SAM are increasingly used for elderly people above age 50. Their fraction among participants has more than tripled from 18 per cent in 1999 to almost 58 per cent in 2003 while that of individuals below age 25 has declined from 12 to 3 per cent. The share of female participants in ABM increased from 36 per cent in 1991 to 65 per cent in 1996 but then declined to 46 per cent in 2003. For SAM, it has been relatively stable between 45 and 50 per cent. Temporary wage subsidies had been used extensively during East German transition in the early 1990s but then lost importance until 1998 when the introduction of SGB III and the new measures it provided reversed this trend. Support of self-employment had only played a minor role in Eastern Germany before 2003. In that year, additional opportunities for support of self-employment have been introduced and the number of recipients more than doubled from about 30,000 per annum in the period 1999-2002 to 72,000 in 2003.

As can be seen from Figure 4, the structure of ALMP expenditure has been relatively stable in Western Germany. Total expenditure was cut significantly in 1994, 1997 and 2003. From 1998 to 2002 it had increased steadily. Labour market training has always played an important role in Western Germany. In 1991, almost 0.6 million individuals participated in labour market training. The development of the number of participants over time is very similar to that in Eastern Germany. There was a sharp decline in 1993 to about 339,000 participants due to abolishment of short § 41a measures. Until 2002, the number dropped further to 273,000 participants and declined considerably to only 160,000 participants in 2003. This development was more than an offset by an increasing number of participants in TM which more than doubled from 265,000 in 1999 to 694,000

in 2003. As already mentioned, in contrast to Eastern Germany, a large fraction of West German training participants does not have any professional degree (31-41 per cent). The number of women and youth below age 25 among training participants corresponds more or less to their proportion of the unemployed. The fraction of long-term unemployed individuals is significantly lower (18-24 per cent) compared to both their share among the unemployed, and Eastern Germany. Another difference to Eastern Germany is the relatively large share of non-Germans among training participants (5-14 per cent).

Employment programmes have only played a minor role in Western Germany. The number of participants in ABM has declined from 83,000 in 1991 to 33,000 in 2003. SAM, on the other hand, only has between 8,000 and 15,000 participants per year. There are also substantial differences with respect to the structure of participants. Compared to Eastern Germany, youth below age 25 and individuals with health problems make up a much larger fraction of participants in ABM and SAM. On the other hand, women and elderly people below age 50 have significantly lower participation rates than in Eastern Germany. The share of long-term unemployed individuals is lower for ABM and higher for SAM. Like in Eastern Germany, temporary wage subsidies have gained importance in 1998. Also, the number of recipients of support of self-employment has tripled from 89,000 in 2002 to 178,000 in 2003. STW had been used extensively in 1993 in response to rising unemployment in that year. Finally, Figure 5 indicates that a substantial part of West German ALMP expenditure has been devoted to 'Other ALMP Measures'. The most important part of these are measures specifically targeted at the disabled and other individuals with health problems. In Eastern Germany, this instrument only plays a minor role.

### **3.1.11 Referral to Activation Measures**

With the exception of counselling and job placement services, participation in ALMP measures is generally defined by receipt of some form of financial assistance from the BA, and jobseekers must apply for this support. For most ALMP measures, there is no legal entitlement to BA support and it is the caseworker in the LEA who decides whether or not an applicant who is eligible will receive financial assistance as well as in which specific measure applicants could participate. In practice, the caseworker usually decides in consultation with the potential participant what measure - given eligibility - would be appropriate based on an assessment of the individual's employment prospects, strengths and weaknesses. Caseworkers have a considerable amount of discretion in their decision. In contrast, some OECD countries use statistical classification methods to assist caseworkers in their decision. Targeting systems like the Frontline Decision Support System in the United States, assign jobseekers based on expected programme impacts. Profiling systems, on the other hand, classify jobseekers by their need for services as defined by some criterion like the risk of becoming long-term unemployed. Statistical profiling is used e.g. in the United

States, Australia, the Netherlands and Australia. See Frölich, Lechner and Steiger (2003) for details. Germany has tested a combination of qualitative and statistical profiling in a pilot project (see Rudolph and Müntnich, 2001).

Before introduction of the Job-AQTIV legislation in 2002, legislators both under the AFG and SGB III had given only few directives for referral of applicants to specific measures. According to § 33 AFG which referred to all training programmes, caseworkers had to use their discretion in accordance with the objectives of the AFG and the specific aims of the programmes. When making their decision they had to consider the situation and development of the labour market, and they had to act based on the principle of economic efficiency. The caseworker had to take into account the aptitude of the applicant for specific jobs and his chances for completing the training successfully (§ 36 AFG). In contrast, for ABM preferential access had to be given to jobseekers with multiple barriers to employment like long-term unemployed or disabled individuals, elderly people above age 50 or youth below age 25 without any professional degree.<sup>60</sup> Under the SGB III legislation, ALMP measures have to be applied in accordance with their specific objectives in order to not only temporarily avoid payment of income support during unemployment (§ 5 SGB III). Until 2001, caseworkers had to base their decisions on the principle of economic efficiency and they had to choose the combination of services that seemed most promising for a specific individual when considering his skills and his chances for successful integration into the labour market. If certain ALMP measures required a choice between different applicants, priority had to be given to those individuals with the best chances for integration. On the other hand, individuals especially in need of assistance such as long-term unemployed or disabled individuals, elderly people with barriers to employment, and individuals returning to the labour market had to be represented in appropriate numbers among participants in ALMP measures (§ 7 SGB III). Women had to be supported proportionately to their fraction of the unemployed (§ 8 SGB III).

The Job-AQTIV legislation has been the beginning of a paradigm change also with respect to the referral process. While still following the principle of economic efficiency and also taking into account the situation in the local labour market, assignment to programmes is now based on individual need for services which is determined on the basis of a newly established qualitative profiling scheme. Based on an assessment of the jobseeker's qualification, mobility, flexibility, motivation, behaviour, specific barriers to employment and an evaluation of the risk of becoming long-term unemployed, individuals are classified into job-ready, counselling and intensive service clients. Special target groups as formerly defined by § 7 SGB III, are no longer mentioned. At the same time, eligibility for some ALMP measures which had been restricted to special groups of people in

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<sup>60</sup> § 2 Anordnung des Verwaltungsrates der Bundesanstalt für Arbeit über die Förderung von allgemeinen Massnahmen zur Arbeitsbeschaffung aus Mitteln der Bundesanstalt. Note that this regulation legalises the practice of cream-skimming

the past (e.g. JCS to individuals with an unemployment record of at least six months), has been extended in order to ensure that ALMP measures can be used as seems appropriate to improve the employment prospects of a specific jobseeker and not be constrained by overly restrictive eligibility criteria.

## **3.2. Italy**

### **3.2.1 Labour market in Italy**

According to the data of the Economic Bulletin №41 prepared by the Economic Research Department of November 2005, employment in Italy continued to grow at the same pace as the previous year. For the first half of 2005, the annual national accounts show the number of persons in work up 0.2 per cent on the previous six months and 0.8 per cent on the year-earlier period. Employment growth was again high in relation to value added. Productivity turned downwards, falling by 0.7 per cent with respect to the first half of 2004.

The Labour Force Survey showed, that 22,512,000 persons were in work in the first half of 2005. The increase over the year-earlier period was 1.2 per cent, more than the growth according to the national accounts. Employment has grown steadily since the mid-1990s, buoyed by moderate real wage growth and a decrease in the cost of utilizing labour. However, in the last two years, given the stagnation of production, the continuous rise in the number of persons in work can be attributed mainly to the regularization of immigrant workers. Their registration with the records office has brought progressively larger numbers within the scope of the Labour Force Survey, leading to a rise in the resident population and observed employment. The regularizations have less impact on the national accounts, which already include an estimate of undeclared immigrant labour.

In the first half of 2005 the employment rate for persons aged 15 to 64 rose to 57.4 per cent from 57.2 per cent a year earlier. The employment rate for women, which remains well below the EU average, increased from 45 to 45.3 per cent, that for men from 69.4 to 69.6 per cent.

The growth in total employment reflected a sharp expansion in payroll jobs. These were up 2.5 per cent on the year-earlier period, of which more than 60 per cent was due to the rise in open-ended contracts, fostered in recent years by the greater incidence of central age-groups and the staying-on of older workers, most of whom have permanent jobs. The number of workers on fixed-term contracts nevertheless increased rapidly (8.7 per cent) and their share of total payroll employment rose from 11.3 to 12 per cent; it is especially high in the South. The incidence of part-time jobs also increased, from 12.5 per cent in the first half of 2004 to 13.1 per cent a year later. All sectors except agriculture were affected and the increase was concentrated among women, with those on part-time contracts up from 24.4 to 25.6 per cent of the total. By

contrast, the number of self-employed workers fell by 2.3 per cent and 141,000, bringing their share of total employment down from 28.1 to 27.1 per cent. The largest decrease was recorded in trade, lodging and catering, where the number fell by 220,000.

In construction, employment expanded strongly, gaining 7.2 per cent or 129,000 compared with the first half of 2004, thanks to the growth in output which has fostered a continuous rise since 1999.

In industry excluding construction the number of workers fell by 0.8 per cent and the share receiving Wage Supplementation benefits increased. According to the survey of non-construction firms conducted by Bank of Italy branches, employment will contract further during the year.

The number of persons employed continued to grow in the service sector, rising by 1.3 per cent or 195,000 on the first half of 2004 and bringing the sector's share of total employment to 65.3 per cent. This result can be ascribed entirely to payroll employment, which rose by 2.7 per cent and more than offset the 2 per cent decline in the number of self-employed workers. The latter was concentrated in wholesale and retail trade and is partly due to the sector's modernization, admittedly somewhat slow, which brought the incidence of self-employment down from 58 per cent in 1993 to 43.7 per cent in the first half of 2005. The service companies interviewed for the Bank of Italy's survey predict a further rise in employment.

Employment growth was confined almost entirely to the Centre and North (1.3 and 1.6 per cent respectively), while in the South, after contracting slightly in 2004, the number of workers rose by 0.3 per cent.

*Unemployment and the supply of labour.* - The seasonally adjusted unemployment rate fell from 7.8 per cent in the first quarter to 7.7 per cent in the second. The decrease was 0.4 percentage points on the year-earlier period and was largest in the South (0.9 points), where it was fostered by a contraction in the labour force. In the second quarter of 2005 the unemployment rate was 4.1 per cent in the North, 6.5 per cent in the Centre and 14.4 per cent in the South.

The labour market participation rate of the population aged 15 to 64 was unchanged from the previous year at 62.4 per cent. While in the Centre and North the rate rose by 0.2 and 0.3 percentage points respectively, to 65.1 and 68.1 per cent, in the South it fell by 0.5 points to 53.8 per cent. The decline in the southern participation rate concerned only women, for whom it fell by 1.2 points, with a reduction in the numbers of both workers and job-seekers.

*Labour costs and industrial relations.* - In the entire economy, gross employee compensation per full time equivalent worker increased by 1.9 per cent in 2005, according to the national accounts, in line with inflation. Actual per capita earnings, not including employers' social security contributions, rose by 2.2 per cent. These overall figures are the result of widely divergent trends in

the public and private sectors: in the former, per capita earnings were stationary at the previous year's level, while in the latter they rose by 3.1 per cent. The slower pace of growth in the public sector can be ascribed to delays in renewing the labour contracts for 2004-2005; those of employees in schools and ministries were only signed in October. The current renewals should bring pay increases into line with the averages for recent years, which have been higher than in the private sector.

In industry excluding construction the cost of labour per standard labour unit rose by 2.5 per cent in the first half over the year-earlier period (3.3 per cent in 2004 as a whole), in line with the increase in actual per capita earnings (2.6 per cent) and contractual wages (2.7 per cent). The slight rise in labour costs was accompanied by a decline of 1.5 per cent in productivity growth, raising unit labour costs by 4.1 per cent.

In the private service sector unit labour costs rose by 3.1 per cent and per capita earnings by 3.3 per cent. The acceleration of labour costs from growth of 2.4 per cent in 2004 was due to the renewal of some major contracts between the middle of last year and the beginning of this (mainly those of wholesale and retail trade, transport, banking and postal workers), which pushed contractual earnings up 4 per cent in the first half of 2005 on the year-earlier period. This acceleration and the further decline in productivity brought the rate of increase in unit labour costs from 3.1 to 4.4 per cent.

In the private service sector currently valid contracts represent 90 per cent of the wage bill, against about 50 per cent in industry excluding construction. In particular, the collective bargaining agreement for metalworkers, which expired in December 2004, has not yet been renewed. The unions have set wage demands of €130 a month, of which €105, representing an average rise of 6.5 per cent, will go to all workers; the remaining €25, representing productivity bonuses, will apply to workers in firms that have not signed supplementary company-level contracts. The employers' association has countered with an offer of €60 a month. Other issues under discussion include working hours, work organization and the rules governing apprenticeship.

In September the collective agreement for some 290,000 workers in the food industry was signed, providing for an increase of €96, or 6.3 per cent, in the two years. As far as schools and ministries are concerned, the renewal of general government contracts for 2004-2005 is now under way. The collective agreements signed so far will provide for a total increase of around 5 per cent.

In the first nine months of the year, contractual earnings in the economy as a whole increased by 3.3 per cent on the year-earlier period. According to available information, on average they should continue to rise at the same pace throughout the year.

### **3.2.2. Regulations of the employment. Legal instruments.**

The problem of legal regulations is represented briefly in Basic Information Report (BIR), Italy 2003. This chapter is fully based on the represented data. The legal instrument in Italy governing employment policy is the law proposed by government or parliamentary groups and approved by the two chambers of parliament.

However, the social partners are involved in determining the overall direction of general policy in the areas of legislative activity and economic policy and planning.

There is no written basis for participation of the social partners, but the latter are involved under a special procedure. The social partners take part in drafting laws and regulations relating to employment at tripartite conferences and meetings. Both are instruments of direct consultation between trade unions and employers' associations on private bills. The 1993 protocol on labour costs and the agreement of December 1998 also systematised participation and involvement of the social partners in the government's economic policy choices. In addition, participation by the social partners was given a further boost following the approval of the 1992 Agreement on Social Policy, annexed to the Treaty of Maastricht and inserted into the Treaty of the European Communities following the Amsterdam Council in 1997. Under this agreement, at both Community and national level the social partners will be involved in transposition of Community directives.

During tripartite conferences, the social partners each express their opinions in a debate between the government and the most representative trade unions and employers' associations. During the tripartite meetings, on the other hand, all the interested parties are heard separately without direct debate.

The government may ask the social partners to present their opinions orally or in writing.

Furthermore, it has become parliamentary practice to frequently seek the opinion of the trade unions and employers' associations on all work-related issues in order to obtain full and detailed information on the subjects of the laws under discussion.

#### **Individual Contract of Employment**

The employee undertakes to carry out the (intellectual or manual) work in question, in return for remuneration appropriate to the type of work, under the authority and supervision of the employer.

A written document is not compulsory for permanent contracts, whereas it is required for fixed-term contracts, training-cum-work contracts and other specific contracts.

Duration of the contract: fixed-term contracts and permanent contracts are available. In performing the work, the two parties must abide by the following rights and duties. The employee is under an obligation to:

- Perform the work himself;
- act in accordance with the conditions stipulated in the contract;
- take care of his working tools;
- be loyal;
- abstain from any activity that is in competition with the employer;
- keep confidential any information relating to the organisation and to the production methods of the company or to make use of it in such a way as to damage the employer;
- obey orders.

The employer is under an obligation to:

- Ensure that the employee is in a position to perform his/her function;
- take the necessary steps to ensure that the working conditions do not adversely affect the physical, psychological or moral wellbeing of the employee;
- take the necessary steps to prevent accidents in the workplace;
- pay the remuneration specified under the agreed conditions;
- assign the employee to those duties for which he/she has been hired;
- provide the employee with information (Law 608/96, Article 9(a): since 1 January 1996, on the date of recruitment employers must provide employees with a signed document detailing the data contained in the employment register).

The employee's responsibility: The employee is responsible under both civil and criminal law for any damage he/she might cause to the employer or to third parties in performing his/her job.

The employer's responsibility: The employer is responsible under criminal law for accidents in the workplace and occupational illnesses which affect his/her employees, and is also liable under civil law if the behaviour which caused the damage was the act of one of his/her employees.

### **Termination of the individual employment contract**

Fixed-term contracts come to an end in one of the following ways:

- Expiry of the term fixed in the contract;
- completion of the task;
- death of one of the parties;
- just cause.

Permanent contracts come to an end in one of the following ways:

- Just cause;
- resignation subject to notice;
- dismissal subject to notice;
- inability to carry out the work assigned;
- death of one of the parties;
- employee reaching retirement age.

However, any clauses providing for termination of the employment contract on the grounds of marriage or pregnancy are null and void.

### **Collective dismissals**

Law 223 of 1991 governs the procedure, formal tasks, preconditions and consultation of trade union bodies if a company decides to instigate collective dismissals.

Rules regarding collective dismissals may also be set out in collective or interconfederational agreements.

Collective dismissals and individual dismissals differ a) in the number of employees dismissed and b) in the reasons for the dismissal itself; collective dismissals are permissible in the case of a downturn or change in the activities or work of the company (in the case of companies with more than 15 employees).

The employer must justify their reasons for the collective dismissal and must notify the trade union organisations accordingly.

The dismissed employees have the right to be rehired if the employer recruits new personnel within one year.

To alleviate the negative effects of collective dismissal, a body called the Wage Guarantee Fund (*Cassa Integrazione Guadagni*) was created to protect employees' wages in the event of a company experiencing a crisis or undergoing restructuring.

### **Contract of employment**

Contracts of employment differ depending on whether they pertain to wage-earners (blue-collar workers) or salaried employees (white-collar workers).

The general provisions relating to the employment contract apply equally to both types of worker. The difference is that under a contract of employment, wage-earners carry out mainly manual work while salaried employees perform mainly intellectual work.

This is nevertheless a distinction which will soon become outdated and obsolete. Collective bargaining has effectively resulted in a new system of vocational classification comprising a single framework subdivided into several 'levels' common to the various categories existing under the law.

### **Trial period**

The trial period is an opportunity for employer and employee alike to confirm whether it is appropriate to continue the labour relationship. During the trial period, either party may terminate the contract at any time without notice or obligation to provide compensation.

The duration of the trial period is fixed by collective agreement and may never exceed the maximum legal limit of six months.

### **Notice**

Notice of dismissal or resignation may be made at any time during the term of a permanent employment contract, provided that notice is given in accordance with the terms laid down in the collective agreement. If these terms are not observed, the defaulting party must pay the other party compensation equivalent to the payment due in respect of the notice period. This obligation does not apply to dismissal or resignation with just cause, or in cases in which circumstances do not permit the employment contract to continue even on a temporary basis.

## **3.2.3 Labour Market Institutions and Processes**

### **Labour relations**

Numerous laws on social security and labour regulations govern employer-employee relationships in Italy.

Regulations vary according to the employers' principal activity, i.e. production, commercial, agricultural, financial or professional. Self-employed agents and sales representatives, as defined under Italian law, are not regarded as employees; however, the employer is obliged to have the representation agreement with such an individual officially registered to provide clear recognition of the relationship for purposes of social security legislation and tax obligations arising from activities carried out under such agency agreements.

Employer-employee relationships are subject to:

1. The Civil Code;
2. the appropriate employment legislation;
3. agreements concluded through collective bargaining;
4. individual contracts of employment;
5. custom and practice.

Collective agreements may apply nationwide for a main sector (e.g. production) or for a particular industry (e.g. textiles), or they may apply only in provinces local areas.

The three main categories of employees are managers (*dirigenti*), white-collar workers (*impiegati*) and blue-collar workers (*operai*). In some branches of activity there may be further categories.

Employers must draw a clear distinction between *managers* and *executive staff who have some managerial responsibilities*. This is because social security contributions by employer and employee alike, the employee's entitlement to a minimum wage (which varies according to length of service), number of days annual leave, minimum notice required for termination of service or dismissal, retirement and death benefits all depend on the employee's category.

Law 300 of 20 May 1970 (the Workers' Statute) sets out the following rights for workers:

- Freedom of opinion;
- no audiovisual equipment may be installed to monitor workers' activities;
- employers may not monitor a worker's fitness for work;
- individual surveys may be made only by using automatic selection systems and must respect the worker's dignity and privacy;
- disciplinary action may only be taken in accordance with established procedures;
- employers may not conduct opinion polls;
- employees may check that accident-prevention regulations are being applied;
- no employee may be downgraded. No worker may be transferred from one unit to another except for proven technical, organisational or production reasons;
- workers have the right to form and join unions and engage in union activity on the premises where they work;
- judges may order the reinstatement of a worker dismissed without just cause.
- union activity, referenda, etc. are allowed. Union dues may be collected through the payroll;
- companies may not suppress union activity.

### **Trade union freedom**

Trade union freedom is a well-defined freedom of association guaranteed by Article 39 of the Italian Constitution. It is aimed particularly at defending the weakest parties on the labour market, i.e. workers, extending as far as to include the constitutional guarantee of the right to strike. Employers' organisations, on the other hand, do not benefit from a similar constitutional guarantee against lock-out (suspension of a company's activities against the collective interests of the workers).

### **Employers' organisations**

Employers are represented by three main organisations:

- The General Confederation of Industry;
- the General Confederation of Trade;
- the General Confederation of Agriculture.

### **Trade unions**

The trade-union movement is strong at worker level. Union membership is not obligatory.

The major trade unions and their political affiliations are:

- CGIL Communist and Socialist (left wing);
- CISL Christian Democrat (centre);
- UIL Socialist Republican (centre left);
- UGL (formerly CISNAL) Italian Social Movement (right wing).

The three most representative trade union organisations (CGIL, CISL and UIL) were grouped into a unitary confederation to pursue common objectives in the interests of all workers.

There are also trade unions specific to an industry or sector of economic activity. Strikes may be called by labour unions, general trade unions, sectoral unions or in-company unions. An industry-wide strike may be applied to a company which has agreed to workers' claims in respect of certain demands, if other companies within the same industry have not agreed to those demands. The metalworkers' union is particularly powerful.

During the last few years, many autonomous trade unions have acquired a higher level of contractual power, especially in the key services sectors (health, transport and education).

### **Collective bargaining**

Unions are most active prior to renewal of a collective labour agreement for a given industry. The agreement is usually renegotiated every three years. After the agreement has been negotiated there is usually a period of relative peace, unless the unions call on the workers to make demands on national issues such as better housing, schools, cost of living or unemployment.

Each industry has a collective agreement stipulating a minimum wage and pay scales. Except in the most depressed areas, very little labour would be available at this minimum wage. Until 1997, the National Institute of Social Insurance (INPS) supplied information and statistics on average wages and salaries in industry.

Between 1975 and December 1991, workers' pay was automatically indexed in line with the cost of living, in the form of compensation for a high cost of living or 'sliding scale'. Under the terms of an agreement drawn up in July 1993 between the Ministry of Labour and the employers' and trade-union organisations on the subject of labour costs, this automatic mechanism has been permanently suspended and the social partners have been requested to determine wage adjustments by means of collective agreements. It was also agreed that pay would be coupled with a planned inflation tax agreed between unions, employers' organisations and the government. This tax is detailed in the economic and financial planning document contained in the Finance Act

All employees in Italy are entitled to an additional month's remuneration (the so-called thirteenth month) payable in December. Furthermore, collective agreements provide for additional payments in some companies. For example, in banking, monthly salaries are paid sixteen times a year and, in the petroleum industry, fifteen times. In commerce, a fourteenth monthly salary is payable in June of each year. In addition, on leaving the employment of a firm for any reason, an employee must be paid a termination of employment allowance.

Services performed over and above the hours stipulated in the contract constitute overtime, which is remunerated at a more generous rate than normal hours. This increase is fixed by collective agreement and depends on the overtime category (during the day, at night, on public holidays), which is also defined in collective agreements.

In particular, the protocol on labour costs of July 1993 contains clauses which represent agreements between the social partners on the following issues: parties to the contract, duration of contract, content of contract, agreed holiday pay and level of contract (national or company level; the latter is linked to company performance on the basis of a range of parameters such as productivity, added value and improvement of services).

### **Employee representation at company level**

#### *Trade-union representation within the company*

Trade-union representation within the company is guaranteed under Article 19 *et seq* of Law 300 of 1970 (the Workers' Statute). It may be implemented at the initiative of the workers in each production unit if it pertains to:

- One or more associations affiliated to one of the most representative national confederations;
- one or more trade union associations which, although not affiliated to the aforementioned confederations, are signatories to national and provincial collective labour agreements in force in the company concerned.

In companies with several production units, trade-union representatives may set up coordinating bodies.

This provision applies to industrial and commercial firms employing more than 15 people and to agricultural firms employing more than five people.

Trade union representatives enjoy some of the same powers as any other elected representative within a private organisation, but some powers are exclusive, such as the right to protect the health and physical wellbeing of workers.

#### *The works' council*

The works' council is made up of all the corporate trade-union representatives or of divisional delegates, office delegates and so forth. It has the following powers:

- Instrumental powers already conferred upon the works committee;
- powers conferred upon corporate trade-union representatives by the Workers' Statute;
- the right of its members to take leave from work or be temporarily relieved of their duties in order to perform trade-union duties;
- the right to engage in collective bargaining at company or production-unit level;
- the right to call a lawful strike at company level.

### **3.2.4. Legal Status of Jobseekers and Unemployment Benefits**

#### **General definition of unemployment and conditions for granting benefits**

##### *General definition of unemployment*

Legislative decree 181 of 2000 (see point 2.5.5) established a new definition of unemployment: a situation in which an individual has no job, is immediately available for work, and is looking for work in the ways defined by the employment services.

##### *Conditions for granting unemployment benefits*

In order to claim unemployment benefit, an individual must report to the public employment office to register themselves as unemployed and must meet certain requirements.

Workers who have lost their job through no fault of their own qualify for standard unemployment benefit if they have been in contributory employment for at least two years, including at least one year during the two-year period immediately preceding unemployment. Benefit is payable for a period of 180 days. As from 1 January 2001, this period may be extended to up to nine months for unemployed individuals aged 50 years or above. As from 1 January 1999, benefit is no longer payable to individuals who resign from their jobs voluntarily.

The allowances consist of a daily benefit equivalent to 40% of the wage/salary received during the three months preceding the period of unemployment. The benchmark wage used to determine this daily benefit is the average wage subject to contributions, and may never be less than the wage/salary stipulated in national and provincial branch agreements related to the number of working days.

Workers who fail to reply to a summons without good reason or who turn down suitable permanent employment that fits their vocational profile, will lose entitlement to unemployment benefit.

Law 223 of 23 July 1991 altered all provisions pertaining to collective dismissals, the Wage Compensation Fund and redundancy.

In terms of the new regulations, collective dismissals are deemed to be dismissals carried out by companies with more than 15 employees and which wish to dismiss at least five workers within

a period of 120 days, in the same province, because of a reduction or a change in their activities or work, or suspension of activities (Article 4 and Article 24 of law 223 of 1991).

In selecting which workers are to be made redundant, companies must either adhere to certain criteria laid down by law (if a collective agreement exists), or must consider workers' family responsibilities, their length of service and the company's technical, production and organisational requirements.

A worker laid off because of cutbacks in manpower is entitled, if he/she has been employed by the company for no less than 12 months (of which at least 6 months must have been effective labour) to a redundancy allowance equivalent to the previous special unemployment benefit, i.e. 80% of the wage/salary which he/she received, but which decreases after the first 12 months. This is equivalent to approximately 64% of the wage/salary.

The maximum durations of payment of benefit are as follows:

- Workers under 40 years of age: 12 months;
- workers over 40 years of age: 24 months;
- workers over 50 years of age: 36 months.

These duration limits are increased by 12 months in southern Italy (*Mezzogiorno*).

Benefit may not be paid for a period longer than that during which the worker was employed in the company.

For each worker made redundant the company must pay, besides the contributions due, six times the initial monthly redundancy allowance to which these workers are entitled. This is reduced by 50% if the redundancy is based on a trade union agreement. Provision is made for specific reductions if the company seeks permanent positions of employment for the workers made redundant.

The regional employment office draws up a list of redundant workers (known as the 'availability list'), which also includes workers who have been laid off following collective dismissals.

Recent regulations include various measures to provide vocational reintegration of redundant workers.

### **3.2.5. Matching Labour Supply and Demand**

#### **Modernising employment services**

Employment services in Italy have been modernised in tandem with two general trends which have characterised reform action in other countries. Firstly, the state monopoly on employment services has lessened - provision was made for this by the introduction of temporary employment agency work (*lavoro interinale*) to implement law 196 of 1997 (the so-called *Treu Package*) and it was *made compulsory* following a ruling of illegality by the European Court of Justice (which ruled, on 11 December 1997, that the monopoly of the Italian government on employment

services was illegal and constituted exploitation and abuse of a position of power) - and the public sector has been reorganised, in particular via decentralisation at local level of management of employment services and simplification of administrative procedures pertaining to the way in which they operate.

*Private employment agencies*

As indicated, the strict blocking of access to the labour market for private operators, as set out in law 264 of 1949, was alleviated by the aforementioned Treu Package and by legislative decree 469 of 1997, both of which enabled access to the labour market for agencies 'supplying temporary work', 'matching labour supply and demand', 'seeking out and selecting staff', and 'providing out-placement'.

Moreover, in this context, provision is made for preventive state monitoring, conducted by selecting 'authorised' private agencies which must comply with objective and subjective requirements in order to be granted authorisation by the state and be listed on the appropriate register.

Firstly, under Italian legislation structural requirements apply to the legal form of the company in question, its organisational and professional suitability for carrying out its activities, and finally, the good reputation of the agency's representatives. Given that there is a certain degree of homogeneity from the point of view of the objective requirements to be met, a higher degree of operational potential is placed on those economic companies intending to perform supply activities. This pertains not only to the agency's territorial distribution (the "activity must be conducted in a number of areas nationwide and in any case in no fewer than four regions"), but also with regard to the minimum number of staff to be employed in its regional branches.

The second general characteristic imposed upon private agencies - that of the financial consistency of the company capital varies (from between a maximum of €516,000 for temping agencies to a minimum of €25,000 for recruitment and selection agencies) according to a hierarchical scale, which, again, places at the top temporary work agencies, which also have an obligation to provide appropriate credit guarantees for workers and social security bodies.

Finally, Italian regulations governing the hiring of private individuals stipulates a third general requirement imposing a negative limit: the so-called 'exclusivity clause' of the company object introduces a system of separation of activities whereby operators may not pursue activities in respect of

which they have been granted authorisation by engaging in other entrepreneurial activities, whether or not connected to the labour market.

Moreover, law 30 of 2003 (the Biagi Law) stipulates that the government must implement the following "indicative principles and criteria". It must:

"provide incentives for different forms of cooperation and links between private and public operators";

"eliminate the burden of having an exclusive company object";

"identify a single system of authorisation or accreditation for public intermediaries, with specific reference to local bodies and private bodies with the appropriate legal and financial requirements, differentiated depending on the type of activity conducted, including the possibility of transferring authorisation and modulating it depending on the legal nature of the intermediary, with specific reference to unrecognised associations or to bilateral bodies or organisations comprising employers' associations and service providers that are comparatively more representative at national or regional level, employment advisors (...), as well as to universities and secondary level secondary education institutes";

"repeal law no 1369 of 23 October 1960 and its replacement with a new regulation, which confirms the penal and civil system for cases of violation of regulations governing private mediation in employment relationships, and which also sets out specific penalties for potential abuse of private mediation and a harsher penalty system in the case of labour exploitation of minors".

#### *Decentralisation of public employment services (SPI)*

In implementing the administrative decentralisation set out in law 59 of 1997 (the Bassanini Law), legislative decree 469 of 23 December 1997 provides for "appointing the Regions and local bodies responsible for exercising labour-market activities", in particular those pertaining not only to employment,<sup>61</sup> but also to active labour-market policies,<sup>62</sup> and leaving the government responsible for general guidance, promotion and coordination.<sup>63</sup>

In particular, the Italian institutional model has, by rejecting the typical agency model adopted in other European countries, opted to delegate authority to the regions, and via the regions, to the provinces. The system of delegating authority to a local level also bestows upon the regions responsibility for

legislation, administrative organisation, planning, assessment and monitoring of employment services, while the provinces are responsible for supplying services via employment centres (CPI).

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<sup>61</sup> In particular, the regions are given responsibility for tasks pertaining to employment (ordinary, agricultural, entertainment, and compulsory, and employment of non-EU workers, homeworkers and domestic workers), and for selective placement within the public administration, pre-selection and matching labour supply and demand, particularly of female workers, and, finally, initiatives designed to boost employment and encourage labour supply.

<sup>62</sup> But with respect to active labour policy, they are responsible for planning and coordinating the wide range of measures which, over the past few years, have characterised both government and regional initiatives (action designed to boost employment and promote matching of labour supply and demand, projects aimed at employment of so-called 'vulnerable groups' (*fasce deboli*), socially useful work (LSU), training and guidance apprenticeships.

<sup>63</sup> The government remains exclusively responsible for monitoring of labour and entry flows of non-EU workers, authorisation for working abroad, settlement of collective disputes and disputes affecting multiple regions, coordinated and integrated running of the Employment Information System (SIL), links with international organisations and coordination of relations with the EU and, finally, excess numbers of temporary and structural staff.

In Italy, no provision is made for a clear management model, but rather each region is responsible for ensuring organisation of its own regional employment systems (*sistemi regionali per l'impiego*), even if within the framework of a number of predetermined bodies.

In addition to employment centres, each system provides for the following:

the Permanent Regional Tripartite Commission (*Commissione regionale permanente tripartite*), a consultation and planning forum, proposes and checks the planning of labour policies for which the regional authorities are responsible. This body must also ensure that the social partners are present and are also represented equally, and that the regional representative responsible for the matter and the equal opportunities advisor (*consigliere di parità*) are represented;

'an institutional body' comprising exclusively institutional representatives of the local bodies responsible for labour-market issues, with the key task of ensuring integration between employment services, active labour policies and training policy;

the Provincial Commission for Labour Policy (*Commissione a livello provinciale per le politiche del lavoro*), chaired by the head of the provincial administration, a tripartite consultation and partnership body of the social partners, pertaining to all the tasks assigned for which the provinces are responsible;

a technical regional body, with a legal personality and independent in terms of assets and accounts, and with important tasks such as providing technical assistance and monitoring with respect to active labour policies, collaboration in integrating labour policies fully (employment services, active labour policy and training policy), guaranteeing liaison with the Employment Information System (SIL), and, finally, delegated to conduct all other tasks conferred upon it by the region (bearing in mind that, among other things, such additional services will be provided on a fee-paying basis for those private companies who request them).

The Employment Information System (SIL) should help to ensure that the new model operates efficiently and in a uniform manner, designed as it is to computerise information on the labour market. The aforementioned Biagi Law also provides for a thorough reform of the system via the introduction of the Continuous Labour Exchange (*Borsa continua del lavoro*).

Finally, in future, the state legislature will have to take into account the new concurrent legislative power of the regions - those to be performed within the framework of the fundamental principles fixed by state law - in the area of 'monitoring and safeguarding employment', and also attributed by constitutional law 3 of 2001, as amended by Section V of the Italian Constitution.

#### *Reform of administrative procedures*

All Italian legislation regarding employment (see 1997 BIR) has been completely reformed via the repeal of many provisions that governed it up until now.

Direct hiring (*assunzione diretta*) is now the general principle governing employment: private employers and public economic bodies directly employ all workers for any kind of employment contract, without the need for authorisation (*nulla-osta*) from the public bodies. Therefore, many standards relating to so-called 'numerical recruitment' (*chiamata numerica*) and 'recruitment by name' (*chiamata nominativa*) have been repealed (see 1997 BIR).

However, there are some important exceptions:<sup>64</sup>

non-EU workers;

Italian workers employed or being transferred abroad; disabled workers;

placement by the Public Administration (*Pubblica Amministrazione*) of workers for qualifications and jobs for which only a compulsory school-leaving certificate is required.

Employers must also notify the appropriate authorities.

Such notification must be made immediately<sup>65</sup> ("Whenever an employment contract is drawn up (...) employers (...) must notify the appropriate authority of such"), and, in addition to applying automatically to employer-employee relationships, also applies to "employer-coordinated freelance work", "workers in a cooperative", and "training and guidance apprenticeships, and all other similar forms of work experience".

Legislative decree 181 of 2000, as amended by legislative decree 297 of 2002, therefore provides for suspension of the system of lists of ordinary and special employment, on which, in the past, workers had to be registered (exceptions were possible for seamen, individuals listed on the national list of performers, and those on regional availability lists and lists of disabled workers).

Accordingly, instead of these lists, Presidential Decree 442 of 2000 stipulated the introduction of the personal data file (*elenco anagrafico*) and vocational record (*scheda anagrafica*).

The list contains personal data on individuals seeking work and who "plan to make use of the appropriate services" - personal data such as residency and address, family composition, qualifications held, whether individuals belong to a protected category, and, finally, their occupational status is recorded.

In contrast, in addition to the information held on the personal data list, the vocational record contains information on training and vocational experience, the worker's availability, and information regarding certification of vocational skills.

### **Employment of disabled workers**

<sup>64</sup> One further exception to the general rule regarding direct hiring is that of the responsibility of the regions. This states that: "The regions may stipulate that a specific quota of individuals hired by private employers and public economic bodies, as well as those individuals hired by public administrations via the selective placement procedures, be reserved for specific categories of workers at risk from social exclusion".

<sup>65</sup> In a clear bid to simplify the administrative burden, different measures are stipulated for temporary employment agencies, by determining a single date each month on which they must forward their information. Temporary employment agencies "must notify the appropriate regional service by the 20th day of the month following the hiring, of the start, extension or termination of the contract of a temporary worker hired during the previous month."

Favourable conditions are offered to disabled individuals to help them start work and this is set out in the obligation on employers to hire a certain number of workers from specific groups.<sup>66</sup>

A new regulation was recently approved - law 68 of 1999 - which replaced the previous law dating from 1968 (see 1997 BIR).

The compulsory hiring quotas for public and private agencies depend on the size of the employer's company:

<b>Number of staff</b>	<b>Compulsory hiring quota</b>
15-35 employees	one disabled worker
36 - 50 employees	two disabled workers
Over 50 employees	7% disabled workers
Over 50 employees	1% widows, orphans and refugees

For private employers employing between 15 and 35 staff, the hiring quota only applies to new recruits.

In order to access the benefits afforded by law 68, disabled individuals who are unemployed must register on the appropriate list held by the relevant authorities. They will then also be entered on a single list according to their points score based on the elements and criteria set by the regions and the provinces.

Employers make hiring requests under the numerical recruitment and recruitment-by-name systems, according to the following table:

Agencies	Recruitment by name	Numerical recruitment
Between 15 and 35 employees	1 disabled worker	
Between 36 and 50 employees	1 disabled worker	1 disabled worker
Over 50 employees	60% disabled workers	40% disabled workers

Employers who, due to the special conditions associated with their activities, are unable to employ the full quota of disabled individuals may, upon presentation of satisfactory justification, apply to the provincial authorities to be partially exempted from the compulsory hiring system. The

<sup>66</sup> The new regulation applies to the following:

- Individuals with physical and psychological disabilities, and those with intellectual difficulties with a reduced working capacity of greater than 45%;
- individuals incapable of work with a disability rate of 33% or higher;
- blind individuals (those who are completely blind or have reduced vision no higher than one tenth in both eyes, with or without aids) or deaf individuals (those who have been deaf from birth or prior to learning a spoken language);
- individuals disabled as a result of war, civil war or military service;
- widows, orphans and refugees and those equivalent to orphans, and individuals listed in law 407 of 1998 (victims of terrorism and organised crime).

provincial employment service may authorise partial exemption up to a maximum of 60% of the reserve quota; this may be increased to 80% for employers operating in the security and surveillance, and private transport sectors. In the event that partial exemption from the compulsory hiring system is granted, agencies must pay the Regional fund for employment of disabled people (*Fondo regionale per l'occupazione dei disabili*) an exemption contribution for each disabled individual not hired of €12.91 per working day.

Furthermore, in the event that the worker needs special support measures to integrate them into the labour market, agencies may ask the provincial offices responsible for setting compulsory employment quotas to specify appropriate agreements. In such cases, the agency makes a hiring request via the recruitment-by-name process. For workers with physical disabilities, the hiring request is always by name and is governed by an agreement in all cases. Via the agreements, which are signed by the workers, employers, provincial offices for integration into the labour market of disabled individuals and bodies promoting integration into the labour market, it is possible to draw up a personalised programme of measures to overcome, as effectively as possible, the obstacles encountered in trying to integrate into the workplace.

Agreements may be of three types:

a) ordinary agreements (*convenzioni ordinarie*), which provide for drawing up a programme to promote effective integration into the labour market, without having to invoke the special terms set out by law;

b) labour integration agreements (*convenzioni di integrazione lavorativa*) to place disabled workers with specific characteristics and difficulties in integrating into the normal labour cycle, which invoke the special terms set out by law;

c) agreements with social cooperatives or self-employed disabled individuals (*convenzioni con cooperative sociali o liberi professionisti disabili*).

The first two types of agreement are concluded between provincial offices, companies and disabled individuals and may be invoked in cases where it is deemed that the worker requires special support measures. The terms contained in the agreement are also determined on the basis of a technical evaluation by the technical committee (*comitato tecnico*) operating within the provincial employment committees (*comitati provincialiper l'impiego*).

The terms which may be agreed include the power of selection by name, operating training or guidance apprenticeships, hiring individuals on a fixed-term contract, or implementing longer trial periods than those specified in the collective agreement. For specific insertion projects, the technical committee may propose adopting derogations to the age limits and duration of on-the-job training

contracts (*contratti di formazione-lavoro*) and apprenticeship contracts to be included in the agreements themselves.

Hiring stipulated in the agreement may be planned according to a predefined period of time during the entire period of validity of the agreements, and may indicate the percentage of placements planned for each reference period.

Provincial offices may stipulate a third type of agreement with private employers governed by the compulsory hiring system and with social cooperatives and independent self-employed disabled professionals, even if they are working for an individual company. Such agreements are aimed at temporary integration of disabled individuals with the social cooperatives themselves, or with the aforementioned self-employed professionals, to whom employers agree to forward work orders.

During the period of validity of the agreement, the appropriate services do not automatically (numerically) place the labour units specified in the agreement and for the entire duration of the programme. In the event of failure by the employer to fulfil the requirements set out in the agreement, the same service will offer placement for the corresponding number of labour units under ordinary means.

The law specifies a penalty system for failure to comply with regulations. Companies with more than 15 staff must send a summary of their labour situation: those who fail to observe this regulation are subject to an administrative fine of €516 for late submission. This figure increases by €26 per day of further delay. After 60 days following the date on which the obligation to hire disabled workers came into effect, for each day during which the quota remains unfilled, the employer must pay €52 per disabled worker not employed.

### **Employment of workers who are not EU citizens**

Immigration and asylum legislation was recently amended by law 189 of 30 July 2002, which mainly amended a number of articles contained in the previous single text on immigration (*Testo Unico in materia di immigrazione*) brought in by legislative decree 286 of 1998.<sup>67</sup>

In order to work in Italy, non-EU workers not yet arrived in the country may obtain a residence permit enabling them to take up employment upon condition of a residence contract (*contratto di soggiorno*) with an employer normally resident in Italy (Italian or foreign). Any such hiring must be one of a maximum number of hirings set annually by presidential decree of the Council of Ministers, announced by 30 November of the year prior to that in question.

Annual entrance quotas are determined annually as follows: Non-seasonal work

- for fixed-term or open-ended contracts of employment;

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<sup>67</sup> The same law 30 included an employment-legalisation provision aimed at non-EU workers working as home helps and domestic workers (Article 33). Subsequently (legislative decree 195 of 9 September 2002), such procedures have also applied to other forms of employment, specifically in the context of illegal immigrants, which has brought the number of applications for legalisation to exceed the 700,000 quota.

- for self-employed workers.

#### Seasonal work

- for seasonal employment.

The duration of residence permits for work purposes depends on the duration of the residence contract and, in any case may not exceed nine months (with respect to one or more contracts) for seasonal work,<sup>68</sup> one year for fixed-term employment contracts, and two years for open-ended employment contracts. Applications to renew a residence permit must be made, in the latter two cases, at least 90 or 30 days respectively prior to the expiry date of the existing permit, and the duration of the renewed permit may not exceed the duration specified by the initial permit issued.

Finally, non-EU workers who have been legally resident in Italy for at least six years may apply (for themselves, their spouse and any dependent children living with them) for an indefinite residence card upon demonstrating that they earn sufficient income to support themselves and their family members.

Entering the country to work requires foreigners to meet a requirement for labour by an employer normally resident in Italy. The employer must apply (by name or numerically) to the immigration counter (*sportello unico per l'immigrazione*) at the prefecture. Following the request, if the provincial employment office is unable to fill the vacancy within 20 days, an entry visa is issued by the appropriate consular authorities. Finally, within eight days of entering the country, the foreigner must go to the immigration counter to sign a residency agreement, which must contain the following details (penalties apply for failure to do so):

- a) a guarantee from the employer that accommodation is available for the worker and that it meets the minimum standards set out by law for accommodation in public residential buildings;
- b) the obligation on the employer to pay the travel costs for the worker to return to his or her country.

If the worker loses their job, they may be entered on the employment list for the remaining period of their residence permit and, except in the case of seasonal work, for a period of no less than six months.

In such cases, the process of finding a job, employment and integration follow the same pattern as those used for Italian workers.

#### **Recruitment to the lower ranks of the public administration**

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<sup>68</sup> "Foreign nationals who can prove that they have come to Italy for at least two years to perform regular seasonal work may be issued with a multiannual permit for that purpose for up to three years". L.30, N°189/2002, Article 5.3(b).

*In general, recruitment to the public administration is by public (competitive) entrance examination open to persons with specified diplomas, or by diplomas and examinations.*

*Article 16 of Law 56 of 1987 introduced an important new aspect concerning recruitment to a public function, for positions of employment which only require compulsory school education, i.e. up to Grade IV. For these positions, a selection is made from unemployed or redundant workers registered on the specific lists with the placement offices.*

*This applies to state administrations, including those with an autonomous structure, national public institutions and those which carry out activities in one or more regions, provinces, municipalities, local health units, and so forth.*

*In order to take advantage of this provision, the bodies concerned must carefully plan their personnel requirements before making their annual applications for selection.*

*The workers involved must wish to be recruited with the qualifications requiring only compulsory school education, and must be registered on the ordinary placement lists, the 'availability lists', or on the lists for placement in agriculture.*

*They must also meet the following requirements:*

- *Be Italian citizens or hold a standard residence permit for work purposes;*
- *be physically able to work;*
- *have civic rights;*
- *be aged between 18 and 40.*

*They must apply to be registered on a special priority list, to be drawn up in December of each year.*

*The order of priority issues taken into account is: family dependants, economic situation and assets, number of years' registration or duration of benefit from the Wage Guarantee Fund.*

*The candidate may be registered on this list with the local employment office in the district where he/she resides or, without changing his/her residence, with another local office.*

*Workers may be removed from the list if they:*

- *Find permanent employment;*
- *find fixed-term employment for more than 4 months in a year;*
- *fail to comply with any of the required conditions;*
- *fail to confirm their unemployed status;*
- *fail to attend a meeting without good reason;*
- *refuse an offer of permanent employment.*

*Placement is conducted using selection tests in the order of the priority listed.*

*As a general rule, the administrations concerned summon the same number of workers as there are positions to be filled.*

*Workers are informed in writing or through publication of vacancies.*

*Workers are then selected according to aptitude tests or practical exercises based on the work to be performed.*

*Workers found to be suitable are named according to the results of the tests and exercises and called to the administration concerned in order of placement.*

### **Measures to match labour supply and demand**

Legislative decree 181 of 2000, most recently amended by legislative decree 297 of 2002, defined a number of measures aimed at preventing long-term unemployment. It also detailed the individuals most likely to benefit from the measures, conditions governing eligibility, and reasons that may deprive individuals to entitlement to them.

Firstly, the following definitions were set out:

*Adolescents:* minors aged between 15 and 18 inclusive, who are no longer subject to compulsory schooling;

1. *young people:* individuals aged over 18 years and up to and including 21 years, or, if they hold a university degree, up to and including 29 years, or any other higher age according to legislation in force in the European Union;

2. *long-term unemployed individuals:* individuals who, having lost a job or having ceased to be self-employed, have been looking for a new job for more than 12 months (or more than six months in the case of young people);

3. *long-term inactive individuals:* individuals who have not previously had a job and who have been looking for work for more than 12 months (more than six months in the case of young people);

4. *women rejoining the labour market:* women who have been employed in the past and who wish to rejoin the labour market after a gap of at least two years; In order to benefit from the prevention measures, the individuals concerned must report to the appropriate authorities - provincial employment commission or approved private agency - to register as unemployed. They must confirm that they:

5. do not have a job;
6. are immediately available for work;
7. are looking for work in the ways stipulated by the relevant authorities.

As such, the decree specifies that in order to match labour supply and demand and to combat long-term unemployment, the appropriate services must provide the following minimum services to the individuals concerned:

a) a guidance interview within three months of the individual registering as unemployed;  
 b) proposals for following a) initiatives to help the individual concerned into work, b) training programmes, c) vocational retraining, or d) any other step to assist the individual in vocational integration:

1) in the case of adolescents, young people and women reintegrating into the labour market no later than four months after the individual has registered as unemployed;

2) in the case of other individuals at risk of long-term unemployment, no later than six months after said individuals have registered as unemployed.

The law also stipulates the following:

a) individuals may continue to register as unemployed if they are employed in work that pays an annual income not higher than the minimum personal tax-free allowance (€7,000 in 2003);

b) individuals shall cease to be registered as unemployed if, without good reason, they fail to attend meetings at the appropriate employment service as part of the prevention measures;

c) individuals shall cease to be registered as unemployed if, without good reason, they turn down a suitable offer of full-time work (either on a fixed-term or open-ended contract), or temporary work either for the fixed term of the contract or until the project is completed, or, in both cases, periods of no less than eight months (four months in the case of young people), that is within the area, radius from home, and travel time limit with public transport set down by the regions;

d) individuals shall cease to be registered as unemployed if they accept an offer of either fixed-term or temporary employment lasting less than eight months (four months in the case of young people).

### **3.2.6. Vocational Training**

#### **Organisation of vocational training**

Until 1972, vocational training activities fell within the remit of the Ministry of Labour, which was involved through both public and private institutions financed by resources from the Fund for the Vocational Training of Workers (*Fondoper l'Addestramento Professionale dei Lavoratori - FAPL*). When Presidential Decree 10/72 came into force, implemented by the law 281 of 16 May 1970, responsibility for vocational training was transferred to the regions, and the Ministry of Labour was responsible for the remaining functions only. However, the FAPL continued to be responsible for financing all activities up to 25%, with the regions providing the remaining 75% of funding.

Following presidential decrees 616 and 617 of 24 July 1977, the remaining responsibilities of the Ministry of Labour were further reduced, while the Directorate-General for Vocational Guidance and Training of Workers (*Direzione generale orientamento e addestramento professionale dei lavoratori*) was abolished and plans were made to restructure its departments internally.

The adoption of Law 845 of 2 December 1978, which can be termed a framework law since it definitively regulates the new structure of measures in this sector, made it possible to determine the remits of the state and the regions, while specifying their respective functions and regulating the corresponding methods of financing. Furthermore, the FAPL was abolished.

*In application of law 845/78, the regions were responsible for:*

- Planning, setting up and financing vocational training activities;
- vocational qualification for the disabled and people unfit for work;
- training activities in prisons;
- training and retraining personnel employed in training activities.

The Ministry of Labour was responsible for:

- Defining and regulating the various categories of vocational functions in order to guarantee uniformity of employment contracts;
- relations with the regions as regards exchange of information and documentation;
- relations with the European Social Fund and with foreign institutions active in the area of vocational training;
- launching and financing initiatives in the area of vocational training of Italians abroad;
- setting up and financing training activities for personnel for technical assistance and cooperation programmes in developing countries;
- study, research, documentation, information and experimental activities;
- transmission to the EU or other international institutions and additional financing of training programmes which may benefit from Community or international funding;
- technical assistance and financing of vocational training initiatives, in agreement with and through the regions in the event of serious local imbalance between labour supply and demand.

The Ministry of Labour carries out the above functions through the Central Office for Vocational Guidance and Training for Workers, the structure of which was reorganised by an ad hoc decree of 10 March 1990.

*Law 196 of 1997 set out the requirements for 'accrediting' training structures responsible for managing activities, relaunched apprenticeship training, introduced 'training' and 'guidance' traineeships, and promoted measures to draw up a system for skills certification and recognition of credits.*

*Subsequently, law 144 of 1999 on initial training (formazione iniziale), introduced the training requirement, i.e. the obligation to take part in one of three channels within the training system (system of education, vocational training and apprenticeship) by the age of 18 years. This provision led on to a process of reform of the initial training procedure. The same law also introduced the new channel of further technical education and training (IFTS).*

*Following approval of Constitutional law 3 of 2001, amending section V of the second part of the Constitution, all responsibility for vocational education and training is bestowed upon the regions, except with regard to essential services and tasks linked to the European Union.*

*Recently, law 53 of 2003 introduced in Italy the right and duty to complete educational and vocational training for at least 12 years. In all circumstances, achieving a vocational qualification exempts individuals from the right and duty to complete vocational education and training. The law also eliminates the distinction previously made between the obligation of remaining in compulsory schooling until the age of 15 years (schooling obligation set out in law 9 of 1999) and the obligation to engage in training activities until the age of 18 years (training obligation, law 144 of 1999).*

*But the reform law standardises the two traditionally separate systems of education and vocational training, which are acknowledged as aiming to achieve the same objectives of promoting growth and valuing individuals and citizens. Accordingly, it provides for a reorganisation and redefinition of various sections of the education and training system, the aim being to ensure that all young people achieve at least one vocational qualification before entering the labour market.*

*Under the new system, after completing lower secondary school, young people may continue to study in the high-school system, run by the state, or in the system of vocational education and training, run by the regional authorities.*

Thanks to the extensive organisational freedom enjoyed by the regions, vocational training differs so much from region to region that in essence there are multiple systems. As such, it is difficult to define a unique curriculum model since the regions have delegated their functions more and more to local administrative bodies (provinces, municipalities) while retaining responsibility for coordination and control.

Furthermore, public structures may run their programmes on the basis of agreements with private institutions. Here, various types of management for vocational training courses are emerging (listed in order of importance):

- Management under private law agreements (especially with institutions of a religious or trade union nature);
- public management;
- direct management (by the region itself);
- management under public law agreements (public training institutions);

- management by delegation (local authorities).

### **Courses**

Courses are structured in the following ways: Preparation for work

- Preparatory training;
- basic qualification for young people who have just completed compulsory education (14 years of age);
- basic qualification for young people between 15 and 18 years of age;
- basic qualification for young people over 18 years of age;
- complementary training in relation to state schools;
- secondary-level training;
- qualification for graduates of colleges of higher education and universities;
- specialisation and further training for graduates of colleges of higher education and universities.

### **Training in the workplace**

- Apprenticeships and training-cum-work contracts;
- training for the employed and unemployed alike.

Training for specific categories of workers (the disabled, women, etc.).

The Ministry of Labour and the regions may, in the course of performing their respective functions in the area of vocational training, call upon the technical assistance of the Institute for the Development of Vocational Training for Workers (ISFOL).

As in all EU countries, in Italy funds from the European Social Fund (ESF) are used to promote in particular those regions which are lagging behind in terms of development. The beneficiaries of ESF initiatives are ministries, the regions, public territorial authorities or economic institutions, cooperatives, and private training establishments.

### **Initial in-company training**

Most young people who do not continue in education look for employment at an early stage. Many of them opt immediately for an apprenticeship; others wait until they have obtained a qualification under a regional vocational training programme or in vocational state institutions. Another method of entering the labour market is the training-cum-work contract (see Chapter III, I-vi.6), which partly overlaps with the above options and is aimed at young people aged between 15 and 29 years (with certain exceptions for areas where serious imbalances exist between labour supply and demand, in which case the upper age limit is increased). The training-cum-work contracts compete, to a certain degree, with regional vocational training courses because of their economic advantages (tax relief, incentives).

*Law 30 of 2003 approved recently on the labour market and employment, provides for reform of apprenticeships giving the regions considerable freedom in regulating training activities and the social partners the same latitude in implementing them; so a distinction is made between apprenticeships for young people aged between 15 and 18 years, with wider training aims, and vocational apprenticeships and those designed to help young people achieve higher education qualifications. The training-cum-work contract is replaced by the integration contract (contratto d'inserimento), under which an individual project can be drawn up to adapt a worker's skills to the employment context.*

### **Further training**

Through the impetus given by the EU, in Italy the focus has shifted away from initial training towards further training because, although their interests may not always be the same, companies, workers and administrative bodies understand better than ever before that vocational training is an investment which benefits everyone, and that their interests do coincide.

*A initial step in this direction was the approval of law 236 of 1993 which made it possible to start structuring a national system of continuing training.*

*The support afforded by law 236 of 1993 made it possible to define a system of continuing training via funding measures such as: company training provided by firms, training for trainers, systems-level support, experimentation in company-level, sectoral and national training supported by the social partners, and experimentation in training upon individual request (formazione a domanda individuale).*

*The laws 196 of 1997 and 388 of 2000 (amended by law 289 of 2002) add to the system a central element comprising the Intersectoral Funds for Continuing Vocational Training (Fondi interprofessionali per la formazione continua), run by the social partners and monitored by the*

*Ministry of Labour and Social Affairs, and funded by a contribution of 0.30% paid by employers. The funds, which finance company-level, sectoral and national training programmes, are also managed by regional administrations within the continuing training system.*

*Furthermore, law 53 of 2000 introduced the right of workers to take 'training leave' to take part in training projects proposed by the worker himself or individually in reference to contractual agreements; in the latter case, provision is made for a reduction in working time.*

The most recent contracts focus more on these issues. It is interesting to note that agreements tend to provide for new ways of exercising the right to education outside the school system (vocational training and retraining, language training, etc.).

*The Istat-Eurostat report CVTS2 (Continuing Vocational Training Survey) revealed that between 1993 and 1999, the percentage of Italian companies with 10 or more staff who had followed a training course had increased from 15% to 24%.*

*In terms of the total number of training activities nationwide, 27% involved companies based in northern Italy, 22% in central Italy, and 15% in southern Italy.*

*In Italy, the low level of inclination towards training is due to the large number of small firms operating, while in large firms, figures are closer to the European average.*

*The same report revealed that in 1999 there were 1,952,000<sup>69</sup> individuals involved in company training programmes (72% men and 28% women), equivalent to 26% of staff in Italian companies with 10 or more staff.*

*Furthermore, reports conducted by ISFOL on the attitudes and habits of workers (2001 and 2002) show that over a two-year period, 31.8% of employed staff and 42.6% of self-employed workers followed some form of training programme.*

### **3.3 Russia**

#### **3.3.1. The Russian labour market**

The Soviet economy was priority driven and planners allocated the resources. There was an excess demand for labour and wages were set centrally. Since the beginning of the break-up of the communist system, the economic, political and social situation has dramatically changed in Russia. Borders have opened up, the market has replaced the previous planned-economic systems and democracy has been introduced.<sup>70</sup> These factors have affected nearly every aspect of life, and the labour market is no exception; a reallocation of companies and labour to the private sector has occurred and there is no longer a dominant state sector providing a safety net against unemployment. Everyday life has been affected for millions of people, although the transition naturally has had different impacts on different regions (Dolinskaya, 2002).

In 1991 the USSR's Law on Employment of the Population explicitly recognized unemployment and created the Federal Employment Service (FES) as the primary government agency dealing with unemployment. However FES soon fell behind in payment of benefits and labour market programs were decreased (Gimpelson and Lippoldt, 2001). The official situation in the labour market however, in terms of unemployment, has been less disastrous than anticipated. Many of the unemployed do not register, in part because the job offered through FES is low-paid and low-skilled, in part because of the commuting distance to the agency (Nivorozhkin 2005a). As also stressed by Grogan and Van den Berg (2001), to obtain unemployment benefits jobseekers are required to register as unemployed at the FES, but

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<sup>69</sup> The report pertained only to industrial and service staff.

<sup>70</sup> It should be noted that in the late 1990s, about one half of all enterprises were still running with losses without being driven out of business. This implies that the soft budget constraints still existed. (Såtre Åhlander, 2005).

benefits are low and often paid after delays, and the eligibility criteria are strict.<sup>71</sup> Furthermore, according to Clarke and Metalina (2000), massive privatisation has brought about little substantive change in the functioning of enterprises. The relatively low level of registered unemployment is also due to wage arrears<sup>72</sup> and underemployment rather than to job loss.<sup>73</sup> (Gaddy and Ickes, 2002). It should also be noted that involuntary temporary redundancy with wage loss has become widespread (see Katz, 2001a).

The use of second jobs is also widespread. Second jobs are mainly performed by men, and the gender wage gap in second jobs is relatively large (Foley, 1997).<sup>74</sup> The second jobs are often informal and hence are not always sufficiently acknowledged in official statistics.<sup>75</sup> Thus, people may be employed without earning anything due to wage arrears, or they may receive their earnings in non-monetary goods. They may have a job but are not working due to underemployment, or they may be officially unemployed but have an informal job and are actually working.

Taken together, these characteristics suggest that employment statistics must be handled with care. As we can see below, the unemployment rate does not deviate significantly from other western countries. Unemployment has increased continuously up to 1998 and has thereafter declined.

**Table 1.1 Trends in Unemployment rate, 1993-2003, per cent**

Year	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
U*	6.0	7.8	9.0	9.9	11.2	13.3	12.6	9.8	8.9	8.6	8.5

\* Unemployment end year, in per cent of labour force Source: EBRD, Transition Report

As far as the employment *rate* is concerned, the rates differ between genders. According to the Economic Survey of Europe (2003), the male employment rate fell by 7.9 per cent be-

<sup>71</sup> According to the law on Employment of the Population in the Russian federation, the duration of benefits is 12 months during an 18-month period. The benefits amount to 75 per cent of the average monthly wage (based on the wage during the last two months prior to the job loss) during the first 3 months, 60 per cent during the next four months and 45 per cent for the last five months. First-time job seekers were eligible for a minimum benefit amounting to the minimum wage (Gimpelson and Lippoldt, 2001). However, according to Nivorozhkin (2005b), although the initial level of benefit compensation is set high, the rules that govern the benefits make sure that only a minority receive meaningful support.

<sup>72</sup> According to Lehman, Wadsworth and Acquisiti (1999) more than half the work force experience some form of interruption of the payment of wages.

<sup>73</sup> Lehman, Wadsworth and Acquisiti (1999) show that the dominant form of labour market adjustment has been the late payment of wages. Klugman and Kolev (2001) claim that among the labour market changes in Russia, reductions in the impact of the time spent in employment and increase in frequency of wage arrears are more important than increases in open employment or the fall in real wages.

<sup>74</sup> Furthermore, workers who have experienced wage arrears, who have been placed on involuntary leave, or who have worked less than full time are more likely to take on second jobs. (Foley, 1997).

<sup>75</sup> Regarding the growth of the informal sector overall, according to Eilat and Zinnes (2000), the size of the shadow economy grew from 19% of GDP in 1992 to 54% in 1997. However, it is difficult to measure the size of the informal sector

tween 1985 and 2001 while the women's employment rate fell by 19.2 per cent (the large decrease in female employment rates mainly occurred between 1985 and 1994).<sup>76</sup> As in other industrialised countries, women in Russia account for the lion's share of part-time employment; more than two-thirds in 2001. The restructuring process has increased the rate of occupational reallocation and the structural changes have entailed occupational mobility. The occupational mobility rates in Russia are only slightly higher than in the US, however. Women in Russia change occupations less frequently than men do. Middle-aged and older people in Russia change jobs more often than in the US. The occupational mobility of middle-aged and older people is likely a result of the structural changes that force people with established careers to change jobs (Sabirianova, 2002).

In the Soviet Union, not only the government but also various enterprises provided social services and were responsible for the payment of a range of benefits. Especially in larger enterprises, it was common for housing, health care, childcare and pre-schooling to be provided by the employer for a nominal fee or free of charge (Gimpelson and Lippholdt, 2001).

Now, the Russian government have relieved enterprises of many formal social responsibilities and the government have also induced campaigns to convince enterprises to reduce their social assets (Mc Auley, 1998). Although many enterprises have continued to provide some services throughout the transition, by the end of the 1990's most enterprises had divested at least some of their social infrastructure.

As a result of the reduction of services (provided by the state and enterprises) during the transition period, the supply of public- and enterprise-based services have been significantly reduced especially childcare facilities (Gimpelson and Lippholdt, 2001). Now Russian households have to weigh the costs of childcare against the value of wages. According to Clarke (1999), women in 1997 were three times as likely as men to consider childcare when opting for their current job. In 1988, 74 per cent of all pre-school children in the Russian Federation were enrolled in kindergartens and nursery schools, whereas the corresponding figure in 1998 was 54% (Samarina, 2001).<sup>77</sup> The availability of afternoon activities and summer

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<sup>76</sup> Katz (2001b) finds from a combination of data that male employment decreased from 37.2 million in 1990 to 33.4 million in 1998. Women's employment fell from 38.1 million to 30.3 million in the corresponding years. However, Katz emphasises that the figures over the years are not strictly comparable. According to the Economic Survey of Europe (2003), the employment/population *ratio* was in 1997, 45.8 for men and 36.5 for women, whereas the *activity rate* (labour force divided by working age population) was 66.7 for men and 50.6 for women for the corresponding year. In 1985 the employment /population *ratio* was 54.7 for men and 50.4 for women and the *activity rate* was 72.6 for men and 63.5 for women. However, as Katz suggested above (2001b), the figures over the years may not be strictly comparable

<sup>77</sup> According to Rossiskii (cited in Katz 2001a), the number of children in nurseries fell by more than one-third from 1989 to 1994. However nativity has also decreased heavily since the dissolution of the Soviet system. Regarding maternity leave, the right to return to the same job was increased from 18 months to 36 in April 1991. The government pays full compensation for 10 weeks after birth. From that time until the child is 18 months there is a low flat-rate benefit, and from 18 months to three years none at all (Katz, 2001b).

campus for school children has also decreased substantially (Katz, 2001a) and public expenditure on health and education, in per cent of GDP has also declined.<sup>78</sup> It should be noted that while death rates have climbed, birth rates have dropped (Manning, 1998).

As far as income is concerned, earnings from formal employment constitute only a part of household total income (Manning, 1998). Another important income source is the production of home grown food. Working at a plot (a dacha) in order to sell but primarily to supply one's own household has become commonplace; household own food production amounts to around 40 per cent of Russia's agricultural output (Seeth et al, 1998). Clarke et al (2000) stress, however, that the rich do not have the time to work on a plot and the poor do not have the money, thus the dacha is not a means of survival for the poorest.

Earnings inequality has increased (Fleming and Micklewright, 1999, Economic Survey of Europe, 2003) and the wage gap between men and women has also been reported to increase.<sup>79</sup> In addition to these changes, GDP growth decreased until 1998. From 1999 onwards, GDP growth has been positive. According to the Economic Survey of Europe (2003), 18.8 per cent of households were living in extreme poverty in Russia in 1998.

**Table 1.2. GDP changes:**

Year	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
GDP*	-5.0	-14.5	-8.7	-12.7	-4.1	-3.5	0.8	-5.3	6.4	10.0	5.1	4.7	7.3

\* Percentage change in real terms  
Source EBRD, Transition Report

The fall of GDP growth was particularly large between 1992 and 1994. However, officially recorded poverty may be exaggerated due to the growth of the illegal sector and of non-reported income. The decline of real income in the formal sector of the economy has been extensive, as has the decrease of monetary transactions<sup>80</sup> (Gaddy and Ickes, 2002).

<sup>78</sup> Furthermore, male life expectancy dropped from 65 years in 1989 to 54 in 1994, recovering to 61 years in 1998. Female life expectancy went from 74 years in 1989, to 71 in 1994 and to 73 in 1998 (Katz 2001b).

<sup>79</sup> Katz found that the female/male earnings ratio fell from 66% in 1989 to 62% in 1993 in Taganrog (Katz 2001b). However, these results can be compared with those obtained by Glinskaya and Mroz (2000) who find that, between 1992 to 1995 the gender earnings ratio was oscillating, rather than showing an upward trend. Newell A., Reilly B., (1996) found that the gender wage gap in 1992 for employed workers in Russia was 30%, and most of this was found to be attributable to gender differences in the returns to characteristics rather than to differences in the levels of characteristics.

<sup>80</sup> The importance of goods and services provided by the employer was also well known in the USSR (Katz, 2001a)

### 3.3.2 Search strategies of the unemployed in Russia

This part focuses on the impact of job search behaviour on the transition from unemployment to employment in Russia. The main objective of the present study is to assess the relative efficiency of alternative job-search strategies for Russian unemployed jobseekers in 1994 and 2000. In Russia, official recognition of unemployment is relatively new,<sup>81</sup> but in accordance with what has been observed in other countries, the prospects for different search strategies resulting in acceptable job offers can be expected to vary between strategies and individuals. Previous Russian studies have revealed large differences in unemployment rates between regions, sectors and socio-economic and demographic groups.<sup>82</sup> Thus, in the present study, not only search strategies and regional differences in labour market conditions, but also variables derived from human capital theory and other social economic variables will be considered.

Empirical studies on search efficiency in Russia are scarce (Roschin and Markova 2005). What make the analysis of search strategy in Russia particularly interesting is the large and rapid institutional and structural change experienced by Russian society and its consequences on individuals' search behaviour. Still, our knowledge about the nature and outcome of job search strategies among Russian unemployed jobseekers remains limited. Due to historical and societal factors there is reason to believe that searching for a job in Russia differs from searching in other industrialized countries. One objective of the present study is therefore to examine whether job search behaviour in Russia actually diverges from other industrial countries or whether the rapid transformation of the Russian labour market during the last decade has entailed some form of convergence in job search behaviour.

#### Search strategies

To obtain a job, an unemployed jobseeker needs to search. The fact that individuals differ in their search strategies may have many explanations. The choice of search strategy might be influenced by the socio-economic characteristics of the jobseekers such as age, gender and human capital endowment (see diagram below). Any specific search strategy may entail not only different outcomes but also different costs in terms of money, time and effort. We assume that the unemployed jobseeker is rational and chooses the most efficient method available, with due regard to the expected return/cost ratio.<sup>83</sup> Thus, each individual is expected to choose the search strategy that maximises the probability of getting a job subject to cost and time con-

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<sup>81</sup> The USSR Law on Employment of the Population recognized unemployment for the first time in 1991

<sup>82</sup> See Smirnova (2003)

<sup>83</sup> This is also in accordance with Holzer (1988) who claims that the most frequently used methods are also the most productive in terms of cost and efficiency. Graham L Reid (1972) finds that the most frequent methods used are also the most common ways to find a job

straints. In addition, the exit rate out of unemployment is likely to be affected by the situation prevailing in the local labour market<sup>84</sup>



Search strategy is defined by the choice of search methods and by search intensity.<sup>86</sup> Search methods may be divided into three main categories: formal, informal and direct search channels. Formal methods include impersonal intermediaries such as public employment agencies, private agencies and advertising notices. The direct method involves contacting an employer (see Huffman and Torres, 2001). Informal methods consist of personal networks such as friends, colleagues and relatives. The sociologist Granovetter (1974) stated that social structure and networks are important components for success in finding a job. He introduced the concept of strong and weak ties based on the frequency of meetings; strong ties are simply people you meet more often.<sup>87</sup> Granovetter (1982) suggests that individuals belonging to the strong ties are more motivated to assist a jobseeker in his/her search for a job. On the other hand, individuals who are belonging to weak ties may serve as a "bridging" device between groups, i.e. weak ties supply more information than that which is available in a smaller and tighter circle. This "bridging effect" appears also to be stronger in higher socio-economic groups. Korpi (2001) found that network *size* is positively related to the probability of getting a job, but he questioned the importance of tie strength. Economists have also studied the role of social networks and contacts. Huffman and Torres (2001) suggest that the use of informal search methods may lead to discrimination, as individual networks have a tendency to differ in influence and power. Social networks may therefore not only facilitate, but also maintain labour market segregation. Furthermore, vulnerable groups such as immigrants may have weaker networks and therefore reduced chances of obtaining work via the informal channels. Formal methods may reduce gender and ethnic inequalities, as they are more open and ac-

<sup>84</sup> To illustrate, Grogan and van den Berg (2001) found that individuals who live in Moscow and St. Petersburg have significantly higher exit rates than individuals in other areas. Earle and Sabirianova (1998) find that individuals in Moscow and St. Petersburg are less likely to be marginalized in the labour market than in other areas in Russia

<sup>85</sup> Human capital is also likely to affect the search strategy *chosen*. This is however not considered in the estimates as we have simply expected that each individual uses the most efficient strategy. (Estimates on determinants of choices were made by grouping the strategies into categories using only formal, informal or direct methods). However, the sample size was too small for these estimates to be reliable. To run a multinomial logit turned out to be impossible due to the different alternatives of strategies and the small sample-size).

<sup>86</sup> As mentioned previously, search intensity is the number of search methods utilised by the job seeker.

<sup>87</sup> Granovetter made a distinction between three categories: people you meet at least twice a week, less than twice a week but more often than once a year, and people you see less often than once a year

cessible than informal channels. However, although a larger share of unemployed who use formal methods may send in applications, the employer can still discriminate when selecting a future employee.

People may use different methods depending on the type of work they are looking for. In addition, a job seeker's search strategy may also depend on the recruitment channel commonly used by employers. The choice of the employer's search channels may also depend on the perception of its efficiency.

According to the human capital theory, greater skills, knowledge and longer work experience entail higher productivity. Empirical evidence suggests that both unemployment risk and duration are negatively correlated to skill and educational attainment. In other words, there is reason to believe that human capital endowment affects search efficiency. Therefore, in order to assess the impact of the choice of search methods on the probability of getting a job, it is important to control for human capital endowment.

During a period of absence from the labour market, human capital may depreciate. This may occur if you are unemployed, sick or caring for children, the elderly or your home for a longer period and are unable to make any compensating human capital investments. Thus, unemployment duration or period out of the labour force is likely to negatively affect the jobseeker's likelihood of getting a job, and therefore his or her search efficiency.

In a recent study, using pooled data from RLMS for the period 1993-2000, Smirnova (2003) analysed the factors affecting the choice of search methods and search intensity in Russia. It appears that Russian women are less likely than men to engage in job search activities, have on average a lower search intensity than their male counterparts and also differ in their search strategies. Older people are less inclined to search for a job and more experienced individuals tend to search less intensively. It should be noted, however, that intensity is defined as number of search methods. People who use a single method intensely are thereby classified as low-intensity jobseekers. Furthermore, Smirnova's results suggest that women are more likely to make use of public agencies. People with more experience are more likely to use advertisements or direct contact with firms. In addition, residents from Moscow and St. Petersburg are more likely to use networks (friends, relatives), and direct contact with employers instead of public and private agencies.

### **Search channels and strategies in Russia**

The Soviet Union was characterized by an excess labour demand. Employers struggled to get permission to employ more staff and almost anyone leaving a job could be certain of finding something else (Katz and Sand 2005). However, labour demand varied according to

qualifications, and gender. Except from distant rural areas it was generally not hard to recruit doctors and engineers, but to find a blue-collar worker was more difficult (Katz 2001). Although female employment rates were high in the USSR, the labour market was heavily gender segregated. Soviet industry demanded unskilled manual labour and women were mainly concentrated to the service sector and office work. (Katz and Sand 2005).

The situation in many industries and regions has changed from excess demand to excess supply of labour and has likely affected the labour market intermediaries and their use. Under the Soviet period, people were generally informed of job opportunities through informal channels, whereas the formal labour market intermediaries existed only for particular categories (Clarke, 1999a). The Labour Recruitment Bureau was never very efficient and had the poor reputation of being a last resort.<sup>88</sup> In 1988 and especially in 1991, the Bureau was given increased authority and responsibilities. As mentioned previously, the 1991 Employment Law recognised the existence of unemployment and established the Federal Employment Service (FES), which was to be financed by payroll tax. FES was established as a decentralized structure with independently operating public agencies (Nivorozhkin 2005).

The Employment Service was in charge of job placement services, active labour market policy programs (training and retraining) and administration of unemployment benefits. Not only the jobseekers but also the staffs were in need of training as they lacked market economy experience and knowledge. A further step toward upgrading and standardising the Employment Service came in 1994 with the introduction of a methodological handbook that provided concrete descriptions of procedures and regulations. The challenge of setting up a full range of labour market programs could not be met, however, due to lack of resources and capacity. The problems were further worsened by the rivalry between the federal and regional authorities for control over resources (Gimpelson and Lippoldt, 2001).

Thus the *public agency* in Russia has a poor reputation; few highly skilled jobs are reported and a steadily decreasing number of jobseekers use the job placement services such as counselling (Clarke 1999b). The Federal Employment Service nevertheless provides some social security services such as child allowance and medical insurance, which may give the poorest jobseekers an incentive to register. Nivorozhkin (2005).

Clarke (1999b) finds that under the Soviet period, the use of *advertising notices* was associated with unpopular vacancies. The traditional way to advertise was to put up a flier near the entrance of the enterprise or at a railway station. This method is still widely used. Today such advertisements are mainly used by private agencies to search for unskilled workers; the pre-

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<sup>88</sup> The low efficiency was due to several reasons: the bureau did not receive any state support, and many enterprises did not report the vacancies to the bureaux. (Clarke, 1999a).

vailing opinion is that you cannot get a decent job through advertisements. As stressed also by Clarke 1999a, advertisements for skilled workers and specialists are mainly found in the press. *Private employment agencies* in Russia are under development; they are mainly concentrated to large cities and recruit primarily professionals. There are two types of private agencies. With the first type, the employers pay the services and the agencies are specialised in recruitment services for employers. The other type of agency provides placement services to the jobseeker and the jobseekers pay for this service. A substantial fee is often charged for job placement services, which limits the accessibility for many people.

### **3.3.3 Recent development in human capital formation and returns in Russia**

Structural and technological changes bring about demand for new types of skills, which may result in large skill gaps between supply and demand. The Soviet economy had an overdeveloped heavy industry and military-industrial complex and an underdeveloped light industry and service sector (Clarke and Metalina, 2000). Thus, during the reform process in Russia, changes in output, employment and required skills were to be expected and the human capital requirements and rewards were likely to have changed. However the restructuring process in the labour market has been slow and the public education system has suffered from cuts in public budgets.

According to Aage (1984), higher prestige rather than higher wages was the principle incentive for investing in education in the Soviet Union. Clarke (2003) finds that the returns to education, in terms of wages, are increasing in Russia and are comparable to those prevailing in other transition countries. These returns are higher for higher educational attainment. For men as well as women, higher education also yields lower unemployment risks, though women have a longer duration of unemployment (Katz, 2001). However, Clarke and Metalina (2000) find that job destruction in Russia during the transition period principally concerned highly-skilled jobs, while job creation mainly concerned jobs demanding lower educational attainment. According to Sabirianova (2002), the increased geographical and occupational mobility in Russia is clearly related to the above-mentioned job destruction and creation process and that people are today more prone to accept jobs requiring less human capital. Thus, the expected returns to education, measured by the likelihood of obtaining a job, may be ambiguous.

Several studies indicate that wages increased with experience in Soviet. Ofer and Vinokur (1992) found that experience and age/wage profile were steeper in the Soviet than in most western countries. According to Oxenstierna (1990), a special seniority bonus was paid in certain occupations and sectors. However, Sheidvasser and Benitez-Silva (1999) claim that returns

to work experience and tenure are nowadays negative in Russia, reflecting a labour market in transition where demand for the good, old-fashioned skills obtained through long experience and tenure has declined. Nonetheless, according to Clarke (1999a), one of the most sought-after qualities of Russian managers is loyalty to the manager; long work experience may signal this quality.

#### **4. Conclusion**

In conclusion one can underline measures which different countries apply to their internal labour market. Unemployment in Germany is still high and has become very persistent. The German labour market still has not recovered from the economic consequences of Unification in 1990. Labour market of east or of west of Germany still differs in many aspects. Especially for Eastern Germany which had an unemployment rate of more 20 per cent in 2003 with high incidence of long-term unemployment, the situation is still worrying.

Traditionally, German labour market policy is characterised by relatively generous benefit payments during unemployment and extensive use of ALMP in times of high unemployment. Germany is among the OECD countries with the highest expenditure on labour market policy measured as a percentage of GDP. Labour market training has always been the most important activation measure and the human capital investment associated with publicly supported training programmes can be substantial. In terms of expenditure, measures specifically targeted at the disabled are also important. In Eastern Germany, employment programmes play an important role for maintaining the employability of jobseekers. Despite substantial expenditure on ALMP, to date relatively little is known about its effectiveness. For employment programmes positive effects have been found for some groups of participants. Additional results based on the new data are expected to be available in 2005.

In response to exploding cost of unemployment and continuing public pressure to solve the unemployment problem, the Federal Government has started the largest social policy reform in the history of the Federal Republic in 2002. The objectives of this reform are, firstly, the reduction of individuals dependent on the UI and social welfare through intensification of job-search monitoring and placement efforts by the public employment service as well as extension of the activation principles anchored in German UI to welfare recipients. For this purpose, one-stop centers for the provision of employment services to all jobseekers independent of their UI status have been set up. Secondly, transparency with respect to how UI funds are spent has been increased. Thirdly, with the aim of more preemptive and more flexible use of ALMP, provision of labour market services has been decentralised and is now based on the jobseeker's individual need for assistance as determined by qualitative profiling which assesses individual strengths and barriers to employment, also tak-

ing into account the situation in the local labour market. Finally, in order to lower the cost of unemployment and to reduce moral hazard, German UI has been made considerable less generous but also more incentive compatible. Work incentives for UI claimants and recipients of social welfare have been increased while sanctions in case of non-compliance with benefit conditions have been tightened. Overall, the reform of the German UI system and labour market policy is an important step in the right direction to solve Germany's unemployment problem as well as the fiscal problems coming with it.

In comparison with Italy and Russia, Germany follows its main principles of care of citizens. According to the data of the Figure 2 Germany spends in several times more than Italy does for its citizens. But the main state policy of Italy towards reduction of the unemployment gives some fruitful results, the employment is stable and the level of unemployment is on the same level with Germany, the average level is 8 per cent. Russia holds the same level of unemployment, nearly 8.0 per cent pro year but with much lower expenses on social sphere and on the problem of the unemployment. It's worth to say, that social measures in Russia are still in the embryo and it is necessary to have time and force to achieve the level of social security system that exists in Germany or in Italy.

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