

# Sharing Risks of Labour Market Transitions: Towards a System of Employment Insurance

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## Abstract

*The increasing polarization of the labour market is closely related to the spread of non-standard employment relationships that largely results from poor risk management of critical transitions over the life course. The question, therefore, arises whether labour market regulation, in particular unemployment insurance, is still properly designed for the new world of work. This article argues for an extension of unemployment insurance towards a system of employment insurance by summarizing the concept of transitional labour markets, indicating the risks that challenge current and future labour markets, laying the theoretical groundwork, and discussing the main features of an employment insurance system.*

## 1. Introduction

The ‘flexicurity’ consensus that the European Commission was conjuring up in 2006 seems to have broken down (European Commission 2006: 111). Its flagship, the *European Employment Strategy*, did not deliver enough ‘good jobs’, so the report on *Employment and Social Development 2011* had to acknowledge an ‘intensified wage polarization’ as the key to understanding rising income inequalities and the risk of poverty at work (European Commission 2012a: 12). Furthermore, the blatant neglect of a proper macro-economic framework, in particular monetary and fiscal policy, led in some countries to a mass unemployment, which many thought was now safely a relic of history. During 2012, youth unemployment in Spain and Greece, for instance, climbed over 50 per cent, an unbearable catastrophe for any social democracy. Finally, the sexy slogan propagated by pundits of Danish

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'flexicurity' 'Protect people, not jobs!' turned out to be too simple a dichotomy, tempting many people to neglect the difference between occasional and systemic jobs. Indeed, there is no need to protect occasional jobs because they contain no investment, but systemic jobs need the protection of substantive mutual investments between employers and workers.

Rising inequality and risk of poverty in work are closely related to the increase of non-standard jobs of low quality or high risks involved. Even during the recession in 2008 and 2010, when full-time jobs for the whole EU-27 decreased by 6.5 million, part-time jobs increased by another 1.3 million. Although temporary jobs declined, too, their share of job recovery in the next upswing year 2011 exceeded 50 per cent. In the same year, 42.5 per cent of young employees were working on temporary contracts, that is a rate three times higher than the average of 14 per cent for working-age adults (European Commission 2012a: 32). This externalization of risks mostly to individuals with weak labour market power raises the question whether labour market regulation, in particular unemployment insurance (UI), is still well adapted to the new world of work.

In the following, I will argue that in many European member-states (MS), especially in those with good employment performance despite the great fiscal and economic crisis in 2008 and 2009 (e.g. Denmark, the Netherlands, Austria and Germany), the UI and active labour market policy (ALMP) already function, to some extent, as a kind of employment insurance, but with a different emphasis in their approaches. These elements could be enforced and enhanced to cope with the current and future challenges of European labour markets. During recent years, however, in many European MS, not least in Germany, flexibility and security were shown to be out of balance for more and more workers. Many life course risks are not at all or at least not fully covered by the current insurance systems. Yet a fully developed system of employment insurance as the cornerstone of social security has to mind *all* critical transitions over the life course. This argument is developed in three steps: First, by briefly presenting the concept of transitional labour markets (TLM); second, by throwing some light on the changing employment relationships and related (new) social risks; and third by laying the theoretical groundwork for risk-sharing and discussing the main features for a fully developed system of employment insurance.

## 2. The concept of TLM

The concept of TLM aims at a consistent framework to give the strategy of balancing flexibility and security a clear normative and analytical direction. The core idea is to *empower individuals* to take over more risk during the life course: First, by not only making work pay but also by *making transitions pay* by extending the social insurance principle beyond unemployment and including volatile income risks connected with other critical events over the life course; second, by making not only workers fit for the market but also by

*making the market fit for workers* by enhancing employers' and employees' capacity to adjust to uncertainties by investing in individual competences as well as in the workplace environment (see Gazier 2003; Gazier and Lechevalier 2008; Jørgensen and Madsen 2007; Schmid 2008).

In a way, the TLM concept reflects a new stage of the ALMP through its emphasis on *active securities*, giving people hand-ups instead of only hand-outs. 'Active' means, first, investing in people versus passive charity, as in pure market economies; and second, protecting people's investments versus protecting jobs, as in pure socialist economies. From this perspective, a generous income replacement for finding a new job is a productive investment (Acemoglu and Shimer 2000), in other words an active security. Subsuming unemployment benefits — if properly designed — under passive labour market policy is a serious mistake because 'passive' connotes only the costs and not the benefits.

The second emphasis of TLM is *life course orientation*. Its concept of 'careers' acknowledges the right of an individual to a development perspective in contrast to the neoliberal concept of 'workfare' that restricts work to an obligation in order to deserve transfers in the case of need. The right to a career also entails a voice in choosing jobs and working conditions in contrast to directing people into jobs in pure socialist economies. Modern labour market services, therefore, have to support *transition securities* beyond the employment–unemployment transition.

This leads to a third emphasis, namely to empower individuals to change from one work situation to another according to changes in the economy, as well as according to individuals' changing preferences or work capacities over the life course. *Citizens should, therefore, have the right to transitions*. 'Work', thereby, includes all activities of social obligatory character, independent of whether they are paid or not. Even participation in collective decision making should be considered as work because exercising voice in work-related decisions is an essential part of economic democracy. Historically, in fact, the first example of a work-related right to exercise voice was seen in the granting of time off to representatives of works councils. Other examples are the right to negotiated leaves of absence for training and sabbaticals, and the right to family-related furloughs, such as parental leave or other care leave (Supiot 2001).

Most people accept changes more easily if the risks are shared justly. That is one of the reasons why the theory of justice plays an important role in the concept of TLM. Elsewhere, I have developed four principles of justice as the *normative pillars of risk-sharing* (Schmid 2008: 224–31): first, *justice as fairness*, which basically means equal access to jobs, and inequality only justified if the lot of the most disadvantaged improves; second, *justice as solidarity*, which means sharing responsibilities according to the type of risks and individual capacities; third, *justice as agency*, which means developing individual and institutional capabilities to enhance individual and regional autonomy, in other words freedom to act; fourth, *justice as inclusion*, which means enlarging risk-sharing communities according to the interdependencies of

economic and social life, that is risk-sharing communities beyond the nation-state in a globalized world.

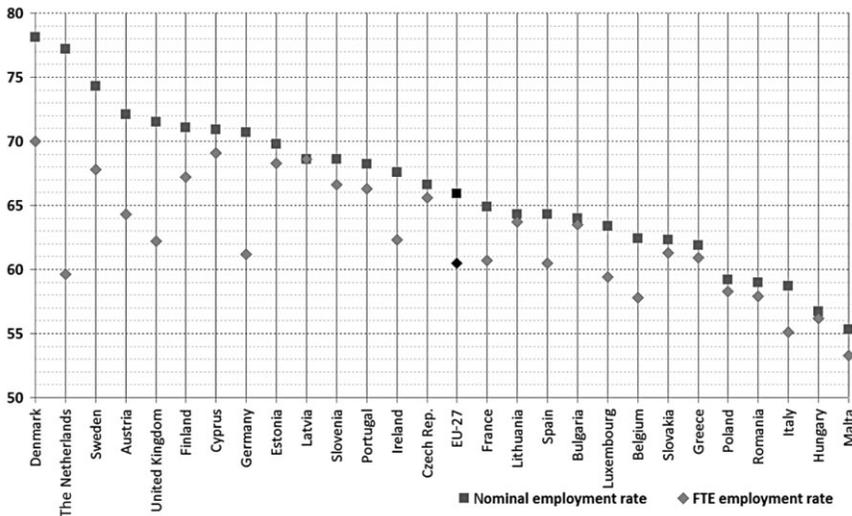
The concept of the TLM has enormous consequences for studying labour markets. First, employment and unemployment have to be considered as a product of stocks *and* flows. An unemployment rate of 10 per cent per year can mean quite different things. It can mean that 60 in 100 persons become unemployed, but remain on average only two months unemployed. But a 10 per cent unemployment rate can also mean that only 10 in 100 persons become unemployed, and stay on average 12 months unemployed. For employment services, these two possibilities represented by the same figure reflect two quite different problems to solve. If most people are only short-term unemployed, employment services have to concentrate on job placement or matching; if a substantial minority is long-term unemployed, however, employment services have to concentrate on training, subsidized employment, protected work or workplace adjustment, or even on public job creation.

Working time also varies over the life course. People move from part-time to full-time and vice versa. Measuring employment by a simple headcount does not take such transitions into account. In Lisbon 2000, the European Commission, for instance, defined full employment as a 70 per cent employment rate (by 2010). Apart from Denmark at the top, the Dutch total employment rate of about 77 per cent far exceeds the official benchmark. But if one measures the Dutch employment rate in full-time equivalents, it falls to 59 per cent, which is far below the Lisbon benchmark (Figure 1).

This discrepancy can be interpreted in different ways: The sceptic view might see the Dutch part-time economy far below its full capacity; the favourable view might consider the Dutch part-time economy as a model for solidaric work-sharing (Visser 2002). The TLM concept welcomes work-sharing as an essential element of risk-sharing, however only under three conditions: First, a developed economy can only afford work-sharing as long as productivity is not affected; second, people working shorter hours or part-time must do so voluntarily, and they must have the opportunity to transit between part-time and full-time as they wish; third, part-time workers must be treated equally in terms of wages, access to social security and employment services.

The transition perspective, however, goes beyond work-sharing or working-time flexibility. It includes transitions between different statuses of work, whether paid or unpaid. People undertake transitions from activity to inactivity, often without changing the formal employment status. In other words, one has to make a distinction between nominal and effective employment. The *nominal employment rate*, for example, in Sweden is about 76 per cent, but Sweden's *effective employment rate* is only about 65 per cent, which means only 65 per cent are actually at their job in a given week. Where are the remaining 11 per cent? In a positive sense, this could mean that about 11 per cent of the active workforce are in education, training, parental or care leave, or even on a sabbatical, and are free of any work obligations for some time.

FIGURE 1  
Nominal Employment Rates (Employed as a Per Cent of Working Age Population 15–64)  
and Employment Rates in Full-Time Equivalent (FTE) in the EU 2008.



Source: Employment in Europe ([http://ec.europa.eu/employment\\_social/eie/statistical\\_annex\\_key\\_employment\\_indicators\\_en.html](http://ec.europa.eu/employment_social/eie/statistical_annex_key_employment_indicators_en.html)).

However, in a negative sense, this could also mean that about 11 per cent of the active workforce are ill or even absent from the workplace by cheating. As a matter of fact, absence rates from the actual job seem to increase with the employment level for whatever reason. The TLM approach, therefore, can also be understood as a concept for managing the gap between nominal and effective employment rates by enhancing an economy's transition capacity in an equitable and efficient way (Korver and Schmid 2012).

The TLM perspective also forces researchers and policy makers to concentrate on *risky events* over the life course, and to look at whether job-to-job transitions lead to *social integration*, *career development* or *social exclusion*. This requires analytical and empirical instruments to study transitions and multi-year transition sequences, to utilize intelligent transition matrices, and to control individual transitions sequences through proper statistical methodologies. Table 1 provides an illustrative example.

This transition matrix shows the yearly transitions of West German women between different statuses of employment or inactivity. The most important result is that women in low-wage jobs have a higher probability of moving into high-wage jobs than unemployed women: 27.3 per cent compared with 16.4 per cent. In contrast, unemployed women have a much higher probability of moving into inactivity than women in low-wage jobs: 30 per cent versus 8 per cent. These figures suggest that the strategy of work first

TABLE 1  
Yearly Transitions of West German Women Aged 20–55 (2000–2006)

	<i>t + 1</i>				<i>Total</i>
	<i>High wages</i>	<i>Low wages</i>	<i>Unemployed</i>	<i>Inactive</i>	
T (Year)					
High wages	87.4	6.8	1.3	4.6	100
Low wages	27.3	61.8	3.0	8.0	100
Unemployed	16.4	20.1	33.4	30.0	100
Inactive	5.9	4.9	4.6	84.7	100
Total	51.1	14.4	3.5	30.9	100

Source: Mosthaf *et al.* (2009) based on the German Socio-Economic Panel.

seems to make sense, however with an important caveat. The chance of getting stuck in a low-wage job is still very high: 61.8 per cent. Too high! The strategic *conclusion for employment services*, therefore, can only be ‘work first *plus* training’. Work first is a meaningful orientation, especially for the low-skilled for whom training *on* the job is more effective than training off the job. Efficiency-oriented employment services, however, have to insure not only a quick placement but also sustainable placements with a high productivity potential.

Finally, the adjustment potential of transitions *within* stable employment relationships (for instance, the transition from full-time work to part-time work, or the combination of part-time work with part-time education or training, and care for children or other dependents) is of great — and often neglected — importance. Such *internal flexibility* has to be considered to be the functional equivalent to *external flexibility*, relevant in particular in view of the fact that most people still strive towards tenured positions. Studies that provide evidence for stable if not increasing job tenures (e.g. Auer and Cazes 2003) are, therefore, not in contradiction with TLM, provided that stable employment contracts allow numerical *and* functional internal flexibility. This view also qualifies the new full-employment target in a different way. The main impulse of the EU-2020 strategy to raise that target to 75 per cent for the working-age population (20–64) stems from the demographic challenge of a declining labour force. TLM’s main motivation for raising the full (nominal) employment target, however, is to allow individuals *and* employers greater variation in effective employment by providing active securities beyond the risk of unemployment, in particular through working-time variation over the life course. The aim is a win–win strategy in which employers gain greater capacity of workplace adjustment, and the workers greater autonomy in the choice of working time and employment.

The TLM concept has stimulated a rich set of empirical research on life course mobility, thereby developing analytical instruments to properly identify modern life course risks (among others, Anxo *et al.* 2007; Brzinsky-Fay 2011; de Koning 2007; Lassnigg *et al.* 2007; Muffels 2008; O’Reilly 2003; Rogowski 2008). The results cannot be reflected at length in this essay, but

the main challenges of emerging social risks must be properly recognized: first, the re-emergence of class-based skill risks; second, the increasing risk of job insecurity, and related to it the increasing risk of income volatility over the life course; and third, the increasing risk of reduced work capacity, mainly due to worsening health conditions or increasing work intensity in the context of the ageing society, and the related need of the increasing labour force participation of seniors with respective workplace adjustments. All three challenges are partly endogenous in the sense that they are also the outcome of governance strategies aimed at taming these new economic uncertainties but tending to shift the risks to the weakest groups in the labour market. The following section briefly documents these challenges.

### **3. Social risks on current and future European labour markets**

The first and most evident risk is that of becoming a loser in the competitive market game due to low education or to skills becoming obsolete. Current labour markets clearly reflect the tremendous unequal impact of the unemployment risk by qualification and the huge differences of employment participation by education. In many MS, the difference in unemployment rates between lower- and higher-educated people is three- to fourfold. Despite the current crisis, people with higher education often face unemployment risks that correspond to the common full-employment definition, that is around 3–4 per cent. Differences in actual market skills cannot fully explain this advantage in the incidence of unemployment; qualification in the form of educational credentials or ascribed competences still seems to be one of the best insurance devices against unemployment.

The risk of skill deficits or educational disadvantage is often aggravated by age. With the exception of a few countries (Austria, Germany, the Netherlands), youth unemployment is at least twice the size of average unemployment; in some countries (Greece and Spain), the adult youth unemployment rate (age 20–29) even surpasses 30 per cent. Obviously, the lack of any experience–knowledge and of work-related social networks puts young adults at a disadvantage when jobs are scarce. On the other hand, outdated skills and shortened time for reaping the returns of firm-specific skill investments considerably lower the re-employment chances of older workers.

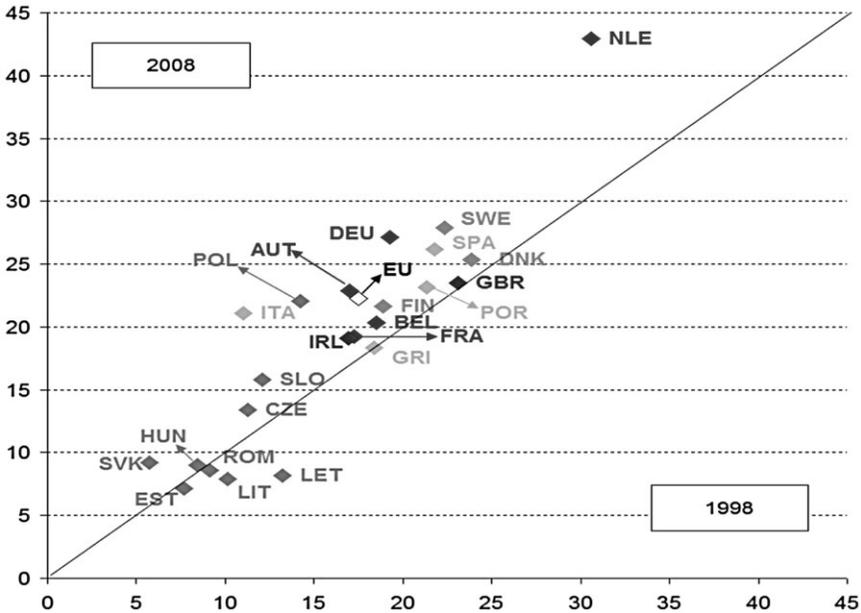
Differences in income opportunities between lower- and higher-educated people through labour market participation are no less striking. Whereas the *employment rates* in the EU-MS of the higher-educated age 20–64 ranged between 78 per cent and 88 per cent in 2010, those of the lower-educated varied between 29 per cent (Lithuania, Slovakia) and 68 per cent (Cyprus, Portugal). The overall gap in employment rates between the lower- (53 per cent) and higher-educated (83 per cent) in the EU-27 is 30 percentage points.

The second main and increasing risk over the life course is job insecurity, reflected in particular by increasing levels of non-standard employment. The current dynamics of transitions tends to lead to new forms of labour market

segmentation. Many people get stuck in exclusionary transitions, especially in low-skilled jobs or in — often precarious — non-standard employment relationships. The graph of non-standard employment in the EU-MS only gives a rough impression of this challenge. The aggregate non-standard employment rates of this figure comprise all jobs in part-time, temporary and own-account work, controlled for overlaps, for example temporary part-timers in temporary work or self-employment (Figure 2).

The comparison of EU-MS reveals three messages: First, non-standard employment rates vary enormously, ranging from 7 per cent (Estonia) to 43 per cent (the Netherlands) in 2008. Through differentiation by gender, the picture — not shown here — becomes more telling. Both the level (EU average of about 15 per cent for men, 21 per cent for women in 2008) as well

FIGURE 2  
Aggregate Non-Standard Employment Rates in Europe, 1998 and 2008.



Note: ‘Non-standard employment’ includes part-time work, fixed-term employment (including temp-agency work) and self-employment (only own account work) controlling for overlaps (e.g. part-time self-employed or temporary part-time workers). The ‘aggregate’ non-standard employment rate is the number of people in non-standard employment as per cent of working-age population (15–64). For example, the aggregate non-standard employment rate of the Netherlands increased from 31 per cent (1998) to 43 per cent (2008); the EU average (about 22 per cent in 2008) excludes Bulgaria, Malta and Cyprus; the new MS display very low and even declining levels. The inclusion of all part-time work as ‘non-standard’ may be, rightly, contested, especially related to open-ended ‘long-part-time’ (20–34 hours), which could (or even should) be counted as an important element of a new ‘standard employment relationships’ defined over the life course.

Source: Eurostat, Labour Force Survey; own calculations.

as the dynamics (EU average of about 2 percentage points increases from 1998 to 2008 for men, and about 4.5 percentage point increase for women) hint to the fact that non-standard employment mainly affects women.<sup>1</sup>

As the clustering (through colours) according to the employment systems shows, the 'social democratic' systems (the champion the Netherlands, as a hybrid system, included) as well as the 'liberal' systems are at the top; the family centred 'conservative' continental systems as well as the Mediterranean systems are in the middle. All of the transition countries (the new MS) — with the exception of Poland — are at the bottom. The aggregate, non-standard employment rate correlates positively (not shown here) both with labour force participation and with economic prosperity in terms of gross domestic product per capita (Schmid 2010: 182–5). This pattern allows the tentative conclusion that a high contractual variety of employment relationships might be a prerequisite for higher prosperity in economic terms. This causal interpretation is certainly far from proved; what is certain, however, is that increasing contractual variety implies more or higher risks.

Whereas self-employment and part-time work show no particular relationship with age, the risk of temporary work is strongly related to youth. On average (EU-27), 40 per cent of the employed aged 15–24 are temporary workers, but only 10 per cent of those aged 25–64 (Berkhout *et al.* 2010: 104). Although the majority eventually ends up in regular work, for many young adults fixed-term contracts (including temp-agency work) turn out to be traps instead of bridges to a tenured career. The consecutive risks, however, depend on the function of temporary contracts. Closely related to qualification tracks (in particular for young academics) or combined with training or replacing a temporary leave, the probability of a temporary contract serving as a bridge to a tenured job is higher than in cases where a temporary job simply functions as a buffer for (cyclical or seasonal) volatile demand. The risk of wage penalties or of ending in a trap also rises with the length or number of individual temporary contracts.<sup>2</sup>

Part-time work was the main driver of increased employment and labour force participation during the last decades, particularly related to women. Denmark and the Netherlands are the only countries where the part-time rate for men comes close to one-third of the female part-time rate, being on average (EU-27) 31 per cent versus only 8 per cent for men (Berkhout *et al.* 2010: 96). There is ample evidence on the opportunities (combining family and work, other elements of work–life balance) as well as the risks (pay penalty, low social security, little training and career promotion) related to part-time. Employers use part-time as a cost-cutting (and productivity-increasing) device, in particular within the 24-hour economy (health, retailing, and hotels and restaurants). From a TLM point of view, the discrepancy between high transitions from full-time to part-time, and low transitions from part-time to full-time, is particularly worrying. Research on low pay attributes a large part of the gender wage gap to this asymmetry and recommends establishing the individual right to reduce working hours in the same job without a negative effect on pay. This may help increase the number of

part-time jobs without the negative effects of occupational segregation that keep women prisoners of low-wage jobs (European Commission 2012a: 19; OECD 2010).

As the clustering above the steady-state diagonal (the implicit time axis) in Figure 2 demonstrates, non-standard employment increased in almost all MS, especially in the Netherlands, Germany and Italy. On the other hand, it is remarkable that most of the new MS not only cluster together in the left corner, but some of these countries, especially Latvia, Lithuania and Romania, even experienced a decline in the aggregate non-standard employment rate. The most likely explanation for this feature is, first, that work in the informal economy (still widespread in these countries) is a functional equivalent of formal non-standard employment; and second, that part-time work (the most important component of formal non-standard employment) does not provide enough earnings for women engaged in formal labour market work in the MS with low income per capita.

The fact that 'social democratic' as well as 'liberal' systems rank high in terms of non-standard employment can be taken as circumstantial evidence that non-standard jobs are related with very different regulatory frameworks. Whereas Dutch or Danish non-standard employees are well covered by employment and income security arrangements, this cannot be said, for instance, for their counterparts in Britain or Germany (Schulze Buschoff and Protsch 2008).

The third expanding cluster of risks are decreasing earning capacities over the life course due to health problems related to ageing, work-related accidents or demanding work intensity. Although it has to be acknowledged that many countries have succeeded in raising the employment rates in the last decade (2000–2009) to a considerable extent,<sup>3</sup> only 11 of the 27 EU-MS reached the Lisbon 'full-employment' target of 50 per cent for senior people (aged 55–64) by 2009. The new EU-2020 'full-employment' target of 75 per cent does not differentiate by age, yet the Barcelona target of increasing the average retirement age from 60 to 65 still holds, and the '*New skills and jobs*' flagship is quite outspoken that a further increase of the retirement age should be envisaged as a response to the demographic challenge (European Commission 2010). 'Active ageing', therefore, has become an accepted strategy (Hartlapp and Schmid 2008), reflected for instance by the fact that between 2000 and the latest available figures, the retirement age has increased by about 1.5 years on average (Eichhorst 2011).

Comparing the employment rates of people aged 60–64 with the new full-employment target reveals large differences between MS. In 2010, the EU average for men was 35 per cent, but only 24 per cent for women (i.e. over 50 percentage points away from the EU-2020 target). The large gap between men and women even holds true for the Nordic countries and the Netherlands, with the noticeable exceptions of Finland, Estonia and France, where elderly women and men are on equal terms. Sweden is the only country that comes near the new target (66 per cent for men, 56 per cent for women). It is evident that varieties in pension schemes and in labour markets situations

account for these large-scale country differences. Both factors have been subject to extensive research, summarized among others by the OECD (2006). Little attention, however, has been given to the spreading risk of reduced work capacities that often comes with ageing. Taking, for instance, the absence rate due to sickness as an indicator of this risk, evidence seems to suggest that this indicator somehow positively correlates with labour force participation, the Nordic countries having the highest incidence (Baumberg 2011: 3; Schmid 2008: 159).

All these (partly new) life course risks must be considered against the backdrop of transforming internal labour markets. From the perspective of risk management, the backbone of traditional internal labour markets (Doeringer and Piore 1971) has been an implicit insurance contract: Employers used to offer the male breadwinner a family wage, job security and lifelong earnings stability in exchange for the acceptance of wages below the productivity level at the peak of the work career. This implicit insurance contract targeted to male core workers is now breaking down without a clear alternative in sight. Many countries with strong internal labour markets (France and Germany) bridged this institutional gap for a while with early retirement schemes and other 'golden handshake' practices. UI, in particular, was made instrumental as a 'social bridge' to retirement. When this led to an overburden of social insurance finances, governments took recourse to paradigm shifts inspired by neoliberal theory. On one hand, most EU-MS introduced stricter work conditionality ('activation') and included more 'employable' people into their UI systems, thereby levelling to some extent the benefits for all risk categories (Clasen and Clegg 2011: 333–45); on the other hand, many MS transformed their pension insurances from benefit-based to contribution-based systems, and from pay-as-you-go systems to funded systems. In this wake, two basic alternatives are under debate or are being practised: Either private insurance elements, such as individual savings accounts, and privately funded retirement schemes are being extended, or the new risks are included into universal social insurance. In the next section, I will argue for the second alternative, yet with some modification allowing greater individual autonomy, and I will present some examples for the further extension of an UI towards a system of employment insurance.

#### **4. Risk-sharing in theory and practice: Towards a system of employment insurance**

Employment can no longer be treated as a binary phenomenon, which means that somebody is full-time employed or unemployed, employed, or retired. The employment relationship becomes fluid as 'people need to be able to carry their welfare state on their back like a snail shell' (Barr 2001: 149). The envisaged extension of the social insurance principle has to take into account the individuality of work–life careers to a greater extent than before, and at the same time has to take care of individual autonomy and protection. The

possibility of revitalizing self-insuring organizations — certainly beyond the conventional escape to the family — also has to be considered, especially in the form of negotiated flexibility and security through collective agreements. The following task briefly summarizes the advantages of social insurance over private insurance principles, demonstrates how far current UI has already gone beyond simply paying benefits, and finally provides a possible framework for the further advancement of employment insurance.

### *Social versus Private Insurance*

Why is unemployment a risk for which the private market cannot provide systematic protection? To be efficient and equitable, private insurance has to meet some conditions. The three most important ones are no moral hazard, no adverse selection and no risk correlation. To start with the last, if risks are correlated or even infectious, as with unemployment, *risk turns into uncertainty*, and there is no way (as it is with stock markets or inflation) to calculate a reliable probability distribution (Crouch 2010: 21), and no private insurance can guarantee liquidity high enough to compensate for the losses of mass unemployment due to fiscal crashes. If risks are unequally distributed, bad risks would tend to overcrowd and good risks would tend to opt out. As a consequence, either bad risks would have to pay high deterrent premiums, or private insurance would not be established. If moral hazard exists and is difficult for informational asymmetries to detect, then control has to be exercised by legitimate power of which private insurers normally do not dispose. These are the reasons why no civilized country has a private UI that sufficiently covers the risk of involuntary unemployment: Only the state can guarantee liquidity in the event of correlated risks that turn into uncertain catastrophes; only the state can force good risks to participate in the insurance or alleviate the burden of premiums for the bad risks; only the state can ultimately exercise legitimate control over moral hazard (Schmid 2008: 231–5).

In paraphrasing the summary by Nicholas Barr (2001: 24), social insurance differs from private insurance in two strategic ways: First, membership is compulsory, thus preventing exit by low risks. The pooling of good and bad risks allows the link between premium and individual risk to be broken. Second, social insurance contracts are usually less specific than private insurance contracts, with two advantages: First, protection can be given against risks that the private market cannot insure; second, the risks can change over time; thus, in sharp contrast with actuarial insurance, social insurance can cope not only with risk but also with uncertainty.

Another argument for social insurance can be added from a normative or legal point of view. Private insurance is based on private law and individual property rights, and can therefore only insure uncorrelated single item risks governed by actuarial principles. Social insurance is based on collective law and human rights, and therefore has to ensure equality (freedom from want) and equal opportunity (freedom to act) independent from the individual

ability to insure against the risk (Sinzheimer 1976: 42–9). Furthermore, there are also macroeconomic advantages, in particular automatic stabilizers (Dolls *et al.* 2011), and the new behavioural economics adds further arguments to social insurance, in particular related to myopic and asymmetric risk perception, leading to the (private) overinsurance of small risks with high probability and the underinsurance of large risks with low probability (Kahneman 2011; Schmid 2008: 214–9; Thaler and Sunstein 2009).

Insuring oneself is also often more costly than pooling risks. The neglect of administrative costs of social versus private insurance among neoliberal pundits is pervasive. Nobody keeps his or her own fire brigade; we all contribute to the community fire brigade instead. Furthermore, precaution or prevention may become costly and may tie up too many resources. For instance, in former times, trading ships used to be accompanied by convoys to ward off pirates; insurance proved to be cheaper. In modern times, many labour markets are heavily regulated to protect employers against opportunistic resignations of core workers (by way of ‘internal’ labour markets) or employees against unfair dismissals (by way of seniority rights). Again, insurance might turn out to be cheaper *and* more equitable in as far as new ports of entry for outsiders are opened.

Of course, as with all insurance, there is a trade-off. On the one hand, insurance has productive functions. People protected by social insurance engage in risky and profitable activities that they would otherwise have not dared to undertake. Risky occupations might not be chosen without the protection of the welfare state, and it would be difficult to find entrepreneurs willing to undertake a risky investment if a debtor’s prison were all that society provided should the venture fail. Eventually, employment-related insurance entitlements turn out to be forceful incentives to find gainful employment, to moderate wages and to undertake training.<sup>4</sup> Without insurance, employers might hesitate to restructure their production portfolio and workplaces if they were unsure of how to compensate their workers whose high firm-specific skills had reduced their employability for the external market. On the other hand, workers who know that a generous wage replacement is waiting if they quit their jobs (there may be a waiting period) might not bother to invest in firm-specific skills; they might even provoke dismissal or make a deal with their employer and fully exploit their entitlements. And by trusting in the social safety net, employers might also take recourse to dismissals instead of investing into the employability of their workforce. This is the moral hazard that exclusively concerns the majority of mainstream economists forgetting the productive role social insurance can play, including properly designed UI (Acemoglu and Shimer 2000).

How to balance productive and destructive risk-taking in a way that maximizes equity and efficiency is an old conundrum of welfare state theory. If people choose more risks *ex ante*, they typically will be more unequal *ex post*. Risk-averse societies may exhibit relatively little inequality, but there is also little economic dynamism. By contrast, risk-taking societies may indeed exhibit high economic prosperity at the cost of high inequality, as the liberal

US regime seems to show. Denmark, however, the ‘flexicurity’ model par excellence, has received increasing applause for its achievement of high risk-taking and low inequality before *and* after taxes (Madsen 2006). It, therefore, does not seem that social insurance necessarily drives the ‘big trade off between equality and efficiency’ (Okun 1975); under certain circumstances, it may well also drive a ‘virtuous marriage between equality and efficiency’ (Schmid 2008: 314–22). One way to shift the balance towards ‘equitable efficiency’ is by enhancing the investment component of insurance-related benefits, as the next section intends to demonstrate.

### *Some Evidence for Already Existing Elements of Employment Insurance*

Spending in the form of ALMP is one way to cope with the insurance dilemma, and employment-promoting measures that go beyond pure matching services can be considered as an employment insurance device. In this respect, the Danish ‘flexicurity’ of low job protection, high income protection through generous unemployment benefits and extensive labour market services to promote employment is already a prototype for employment insurance. Employment subsidies (in particular for the elderly) and continuous training or education for adults thereby play an important role. It is interesting to note that Denmark is also one of the few countries that spend relatively more for ‘active’ than for ‘passive’ labour market policy measures. Other countries belonging to this league are Sweden and — surprisingly — Poland, as well as the UK, yet they all have quite a low absolute level of expenditure. Even Switzerland (characterized by high employment rates and relative low unemployment) combines, like Denmark, high market flexibility through decentralized wage bargaining and relatively low employment protection regulation with a strong focus on active labour market policies. It is also one of the few OECD countries where the funding of labour market policies is triggered by changes in the level of unemployment, since the federal funding of the public employment service (PES) varies annually with the number of (projected) registered unemployed (Duell *et al.* 2010: 43).<sup>5</sup>

The change of perspective from unemployment to employment insurance also draws attention to the direct or indirect employment impact of social insurance systems not directly related to the labour market, such as, for instance, pension systems. In fact, we observe that governments put more and more emphasis on the ‘activation functions’ of such systems rather than seeing, using or even exploiting them as escape routes for deficits in the systems of labour market insurance. It is not by accident that in many countries, the extensive use of part-time work finds its parallel in a citizenship basic income in old age, which is independent from the work history of a person, for instance, in Switzerland, Denmark, Sweden and particularly in the Netherlands (Visser 2002). In 2002, social partners in Finland reached an agreement on extensive pension reforms, thereby introducing explicit elements of employment insurance. People can retire flexibly at the age of 62–68. In this period, the accrual rate increases from its standard rate of 1.5 per cent

per year to 4.5 per cent for those aged 63–68; the pension entitlements are no longer calculated on the income of the last 10 years but are instead based on lifetime earnings, and the scheme is automatically adjusted to the change in life expectation (Hartlapp and Schmid 2008).

A final example is enforced working-time variation through economic up and down cycles, and the insurance of respective income volatility instead of costly and inequitable hire and fire. In the meantime, this kind of employment insurance is fairly widespread and was extensively used during the last recession (Eurofound 2010). Although known in some countries as *part-time unemployment benefits* and often subsumed under ‘passive’ labour market policy, the following excursion based on the German example will demonstrate that short-time work (*Kurzarbeit*) is far from being ‘passive’; as a matter of fact, *Kurzarbeit* could be seen as the paradigm of employment insurance if some of its risk-sharing elements were to be enhanced by investive components.

German *Kurzarbeit* goes back more than 100 years. Today, there are three different types: *cyclical short-time work* to maintain employment in cyclical troughs; *seasonal short-time work* helps construction workers, in particular, to overcome income risks during bad weather and cold winters; and *structural short-time work* helps companies in restructuring to prepare redundant workers to find a new job. Workers have a right to short-time work. Even works councils are entitled to apply for short-time work at the PES. Reduced wages are compensated like unemployment benefit, which is by 60 or 67 per cent replacement of net income.

In 2009, about 1.2 million workers went on short-time work and reduced their working time, on average, by about one-third by maintaining their full-employment relationship. Yet other instruments of internal flexibility were also used, for instance, the reduction of overtime, the melting down of accumulated working-time accounts, and the reduction of working time by utilizing time *and* ‘wage corridors’ provided by collective agreements. These corridors allow firms to deviate from standard collective agreements, for example, by reducing under certain conditions working time *with* respective cuts of wages; so ‘wage corridors’ are an instrument of both: working-time *and* wage flexibility. Most agreements provide for 10, some for 20, per cent deviation from the standard weekly working time (e.g. a corridor of 32–40 hours), but wages are not allowed to fall below this level. Although, for instance, the volume of working time fell in the machine tool industry by about one-fifth, the employment level was practically maintained; at the end of 2010, only a few short-time workers remained, and the working volume reached the level before the crisis. The use of these internal flexibility instruments combined with various elements of income security is the main reason why Germany coped with the crises without substantial increase of unemployment (Möller 2010).

Yet, before praising this as the ‘German job miracle’, the balance of this kind of risk-sharing has to be carefully assessed. *For the workers*, the advantages are quite clear: Their wages are insured in a double form: by inclusion

into the UI system and by collective agreements that top the regular wage replacement up to 90 per cent. In addition, short-time workers maintain their jobs, their qualifications and their social networks. Problematic are the low incentives for activation and mobility, and current regulations do not legally entitle short-time workers to qualification measures.

*For employers*, the most immediate advantage is the maintenance not only of skilled workers, but also of workers who are loyal and co-operative; the opportunity costs of recruiting, for instance, high-skilled craft workers or engineers are estimated to amount up to €32,000. Short-time work allows a much quicker reaction to demand fluctuations than dismissals because dissolving employment contracts needs more time and implies higher transaction costs than just reducing working time by maintaining the employment contract. Short-time work also offers employers the opportunity of *strategic waiting* in the face of uncertainty, which means ‘workforce liquidity’: Nobody knows at the beginning how big the drop in demand will be and how long this will take. Short-time work is a reversible instrument, dismissals are not. Short-time work also provides an opportunity to adjust the organization of work precisely according to the specific tasks to be reduced or expanded. The government increased this flexibility by relaxing the conditions that allowed especially small firms (for instance, logistic enterprises and suppliers of large firms) to use the scheme to a larger extent than in former times. The remaining fixed costs per short-time worker of between 24 per cent and 46 per cent, depending on the size of government subsidies, can be problematic; for the society, however, these remaining fixed costs are an effective incentive to not misuse the system. The low incentives for employers to improve the long-term employability of their workers are also problematic; they do not even have the right to instruct workers in the short-time work phase.

*For the society* or the state, the first evident advantage is the avoidance of open unemployment. The German short-time working scheme, together with other working-time adjustments, prevented open unemployment by about 1.4 million workers. This is not just manipulating statistics. This form of job security first maintains high purchasing power in times of otherwise falling demand, and second avoids ‘angst’, meaning the panic reactions of workers, for example an unreasonable saving that might reduce effective demand leading to a vicious circle. For the *government* and the PES as social insurance principals, short-time work offers a lot of discretion to fine-tune the scheme as the situation develops. The government used this discretion by extending short-time work up to 2 years, giving employers a comfortable planning horizon, and the PES gave employers a great deal of freedom in implementing the scheme. It could do so because both the managers of private companies and public employment agencies had, over a period of time, gained not only experience with this instrument but also mutual trust relationships.

The problematic features, however, are not just minor. Each job protection scheme weakens the situation for ‘outsiders’ and may slow down structural change that might be necessary in the long term. Also the costs of such schemes are not minor. The risk-sharing community of all workers, for

example, spent about five billion euros for the minority of short-time workers, and high social contributions are always hidden costs of production. Finally, the government complemented this risk-sharing community by subsidizing social security contributions and by offering a large stimulus package through a so-called wreck-bonus. People owning a 9-year-old car could deposit their car in a wrecker's yard and take home a new car subsidized by €2,500. This cost the society another five billion euros and contributed, of course, to high public debts.

Short-time work as an instrument of employment insurance, therefore, has clear disadvantages compared with external flexibility covered by UI. State subsidies may shift the costs to taxpayers or to marginal workers; job security may maintain non-competitive industrial structures and lead to jobless growth or new job creation only in a non-standard form, especially temp-agency work. In implementing short-time work, Germany failed in at least two respects from a TLM point of view: the incentives for training during short-time work are too low, and a corresponding flexible training infrastructure is still missing. All in all, however, the balance is positive. Yet there is a clear need to complement this instrument with other elements, especially with lifelong learning, which can also be seen as an opportunity to take a definitive step forward to a system of employment insurance.

### *The Challenge of Lifelong Learning*

Why should the state, as the social insurance principal, get involved in the game of sharing risks related to vocational or educational transitions over the life course? The first reason is savings restrictions. Numerous studies have shown that workers with the greatest need for continuing education and training are especially the ones who will not be able to save enough for substantial investments. Yet only social insurance entitles you to cash in your insurance largely independent of how much you have already saved or contributed. Largely neglected are comparable restrictions on the demand side: Many enterprises, especially small- and medium-sized firms working at the profit margin, will not save for investing in the employability of their workers or work organizations. Under competitive pressure, they will take rescue to cost-cutting measures, which means to price competition instead of quality competition needed in a globalizing world (for this section and the following, see Acemoglu and Pischke 1998; Chapman and Ryan 2005; Diamond 1999).

The second reason is *capital market restrictions*, again on both sides of the labour market. The market does not loan to those who most need credit for continuing education and training. Unlike, for instance, housing loans, education or training loans have no collateral for the bank to sell if the loan recipient defaults on repayment. The same holds true for enterprises with weak capital endowments. Studies show that non-participation of enterprises in the lifelong learning of their employees is strongly related to the lack of targeted budgets for training and to the lack of professionals devoted to personal development.

A third reason is *poaching or free-riding* related to the well-known theorem of the prisoner's dilemma: It may be rational for both sides not to co-operate. Firms who invest in their employees might not reap their returns because other firms will poach their skilled workforce, and workers might opportunistically run away to the competing firm offering higher wages. Of course, clauses in the employment contract might control for poaching or free-riding. However, such clauses might involve high transaction costs leading to an underinvestment in life course employability.

Fourth, this tendency will be enforced by *mobility restrictions* related to internal labour markets. From institutional theory, we know that internal labour markets provide a kind of wage insurance for workers, especially through seniority wages, and for employers a kind of loyalty insurance. In the future world of work characterized more and more by network labour markets, this rationale for implicit insurance, however, is weakening. Furthermore, firm-specific and sector-specific investments in lifelong learning unduly restrict job-to-job transitions between firms and sectors. This does not mean that the rationale for internal labour markets disappears completely as my remarks on short-time work made clear, but it has to be enhanced by *internal transition capacities* through lifelong learning.

Yet there are further behavioural reasons that call for a universal lifelong learning insurance, however, to be implemented in the form of negotiated flexibility and security. The first reason is *uncertainty of returns for workers*. Our cognitive map values what we already possess much higher than what we might expect from risky investments (Kahneman 2011: 289–99). This endowment effect is more relevant for low-skilled and low-income earners than for the high-skilled. The resulting risk aversion can only be overcome by extending the expectation horizon through conditional job security or through employment security; legal rights to lifelong learning and possibly legally guaranteed minimum levels of education would also extend the expectation horizon; finally, the certification of acquired new skills belongs to this solution which, ideally, would have to be put into the context of learning modules, leading to a promising career perspective.

On the other side of the coin, *employers* having to make the decision to invest in their low-skilled workers *face the high risk that the returns of their investments might be zero or small* due to low learning capacities. Only higher education levels signal higher learning capacities (both in terms of cognitive abilities as well as in terms of learning motivation). This is the rationale for the consistent empirical findings that lifelong learning strongly correlates with education levels: The participation rate of the high-skilled is, on average, 40 percentage points higher than for low-skilled across OECD countries; the overall participation rate of high-skilled varies between 20 per cent in Hungary and 90 per cent in Sweden; for low-skilled, between 2 per cent in Hungary and 55 per cent in Sweden (OECD 2011: Chart A5.2). This risk aversion of employers can only be overcome by co-financing investments in low-educated workers by providing a corresponding training infrastructure that ensures positive returns for these target groups, and by a universal

obligation of employers to contribute to a training fund targeted at unemployed or low-skilled people.

Finally, there are *information uncertainties* for both: labour supply and labour demand. Research consistently shows that workers are often faced with complete intransparency of the training market, and that employers do not know what kind of skills they should invest in. More important, these uncertainties beget another uncertainty: The players of the lifelong learning game — workers, employers *and* the state as the representative of externalities — do not know beforehand where gains are going to accrue and where losses must be incurred. This observation holds true at micro- and macrolevels alike. The veil of ignorance, the insurance situation, is a given.

The solution to these information uncertainties can only be in learning by monitoring (Sabel 1994) through establishing *learning communities* at the local or regional level, in which all relevant actors — schools, training institutions, employers and social partners — get involved. This involvement, however, needs to be organized in a form that makes actors committed and responsible (Korver and Oeij 2008; Korver and Schmid 2012; Schmid 2011: 105–12).

*Covenants* are an established form of such negotiated flexibility and security, well-known under this term in the Netherlands. Best practice in continuing education and training is not common knowledge yet, but it probably already exists *de facto*, for instance, in Denmark (Lassen *et al.* 2006), and it may be the secret of successful local or regional labour market pacts or local strategic partnerships (Burroni *et al.* 2010). It is also likely to evolve, for the urgency of this overarching common goal at all levels of governance is pressing, not least in relation to the flagship initiative ‘*New skills and jobs*’ of the new European Employment Strategy in the frame of EU-2020 (European Commission 2010, 2012b). Covenants are written agreements between two or more partners to reach a common goal through *procedural security* considered as fair by all involved parties. In many cases, the state is involved as an initiating and co-signing partner. Unlike private or public contracts, covenants are voluntary and require no legal framework. Partners, thus, retain an exit option if the risk-taking appears excessive. On the other hand, such agreements must also contain voice options to solve problems step by step as they arise. Because the balance of costs and benefits might change at each step, the partners involved in the game must trust in the possibility that corrective measures can be taken in pursuit of the common goal through a fair process of renegotiations.

## 5. Concluding remarks

Many of the new labour market risks go beyond unemployment for which UI was once established. This development has been going on for a long time, and as a matter of fact many countries have already adjusted to this situation by extending the spectrum of risks included into their social insurance — within or complementing their UI system. In this essay, I have argued that it

is high time to go a step further. There is a need for a systematic shift from simply insuring unemployment towards a system of employment insurance that covers risks beyond unemployment, in particular risks related to critical transitions over the life course: transitions between full-time and part-time work, transitions between one occupation and another, transitions between care work and gainful employment, and transitions between full work capacities and partial work capacities. Many of these transitions can or could be organized within stable employment relationships, thereby avoiding the exclusionary tendencies of non-standard employment. The concept of TLM aims to provide at least some strategic elements for such a paradigm shift, which can be summarized in four points.

The first element is to establish a *general labour force membership status* through universal social rights and duties that include all kinds of work, paid and unpaid. Examples are the right to change working time over the life course, that is moving back and forth between full-time and part-time, and the right to some replacement of lost income due to reduced working time, especially in cases where the reduced income capacity is due to unpaid care work. The second element is to establish a *career orientation* over the life course through *making transitions pay* and insuring life course risks beyond the risk of unemployment. The most promising example is public support of lifelong learning, especially (but not exclusively) for the low-skilled; the benefit to the society would be enhanced mobility, in particular in the form of mobility chains that open up new ports of entry for outsiders. Another example would be wage insurance, providing some income protection when a change from a higher to a lower paid position becomes necessary. The third element is to overcome inequalities and risk aversion through *capacity building*, for instance, through stepping stones, reasonable adjustment of workplaces and active securities like drawing rights for investing in human capital. With this perspective, unemployment benefits have to be considered as 'active' and not as 'passive' security: as an investment in the search capacity of individuals and in the matching capacity of the labour market. The fourth element is to *transform danger into trust* through negotiated flexibility and security, in particular through establishing learning communities in which not only social partners but also other regional key actors agree on specific employment objectives, including not only job creation but also issues of lifelong learning and the humanization of workplaces. Obviously, revitalizing and renewing 'industrial relations' would be key in establishing an equitable and efficient system of employment insurance.

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**Notes**

1. For a more detailed analysis of non-standard employment in Europe with a richer set of figures, see Schmid (2010); for the American context, see Kalleberg (2009).
2. Robust evaluation evidence on the incidental as well as consequential risks of temporary contracts is still rare; for some selected pioneering work, see Gebel (2009), Hartman *et al.* (2010), Cockx and Picchio (2009), and Kinnunen *et al.* (2011).
3. For instance, Germany by about 18, the Netherlands by 17 and Finland by about 14 percentage points; some of the new MS (e.g. Bulgaria by about 25, Slovakia 18 and Latvia 17 percentage points) even outperformed the old MS.
4. A persuasive proof through simulations on the basis of an equilibrium model and employment policy characteristics of the (successful) Nordic model is provided by Kolm and Tonin (2012).
5. Earlier evaluations often found no or little positive impact of training on re-employment. Card *et al.* (2009), however, found in a meta-evaluation of 199 studies on labour market policies that more recent evaluations covering medium- and long-term effects found significantly more positive impacts in particular for training measures.

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