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Sickness, Disability and Work
Breaking the Barriers – Vol. 3

Chapter 5

The Individual's Perspective: Financial Incentives for Taking up Work

One of the main objectives of current disability benefit reforms in all four countries is to increase incentives for persons with disability to take up or to remain in work. Disability and other public benefits are an important source of income for people with disability, especially in lower income groups. While these benefits are particularly targeted in Ireland, they provide lower net replacement rates than in the other three countries.

The design of these benefits in combination with income taxation can create work disincentives. Average effective taxation is high in all four countries and reaches 70% to 90% with a few exceptions. Different in-work benefit elements are operated to overcome this problem but are either too small in size (Finland), have a take-up problem (Ireland) or are effective only for higher-income groups (Netherlands).

The prime aim of disability benefit policies – in conjunction with other benefit policies – is to prevent large financial losses and poverty risks for people who experience long-lasting health problems or disability. At the same time, governments need to ensure that these policies are balanced enough so as to avoid "benefit traps", *i.e.* situations in which a possible take-up of work actually penalises the persons who intended to do so. This chapter looks at this income adequacy/work incentives dilemma. It shows that, in a non-negligible number of constellations, benefit systems fail to achieve one or the other objective and highlights examples and suggestions to avoid such situations. The first section looks at the "attraction" and adequacy of disability benefits *versus* other working-age benefits, in particular unemployment and social assistance benefits. Section two analyses financial consequences for people with disability when taking up work and discusses incentives for persons on partial disability benefits. The last section concludes.

5.1. The "attraction" of disability benefits

A. The relative importance of disability benefits and their distribution

Average gross disability benefits are around 35% to 41% of average national gross earnings in the four countries under review (Chapter 1). Persons with disability rely, however, on a multitude of income sources: Other public benefits often play a major role, but other sources also include own earnings, capital income, and income from savings and private transfers. Furthermore, the resources of other household members with whom the person with a disability is living contribute to (or, in their absence, put a burden on) their economic well-being.

This "income package" differs, however, between countries. In all countries, labour income plays by far the most important role, accounting for as much as 78% of the income of persons with disability in Denmark and 58% to 65% in the other three countries (Table 5.1). The share of labour income in total incomes remained stable in Ireland and very slightly decreased in Denmark and the Netherlands in the past ten years. In Ireland and the Netherlands, this is in contrast to the development for persons without disability: their labour income share increased by 4 to 6 percentage points (no comparable trend data are available for Finland).[1]

Second, public social transfers are an important source of income for persons with disability. Their share in total income is about three times that for persons without disability. It should be noted that various non-disability related public benefits such as old-age pensions and family benefits are as important as disability benefits – the latter account for less than half of all transfer income of people with disability in all countries (data not shown). Total public transfers make up for 18% of all income of people with disability in Denmark, 33% in Ireland and 40% in the Netherlands. The low figure (13%) for Finland is explained by the fact that all earnings-related pensions are counted within "private transfers and capital income".[2] This income source, together with "other income" is less important in the other three countries and the share decreased in Ireland and the Netherlands.

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Table 5.1. **Earnings constitute four-fifths of income for persons with disability in Denmark**

Income composition by disability and employment status, 2005 and changes since 1995[a]

	Employed with disability		Not employed with disability		All people with disability		No disability	
	Level 2005	Change 1995-2005	Level 2005	Change 1995-2005	Level 2005	Change 1995-2005	Level 2005	Change 1995-2005
Denmark								
Labour income	94	1	46	–6	78	–2	90	–3
Public social transfers	3	–9	47	–1	18	–6	6	–5
Private transfers, capital, other income	3	8	7	7	4	8	4	8
Finland								
Labour income	83	..	35	..	65	..	78	..
Public social transfers	7	..	24	..	13	..	9	..
Private transfers, capital, other income	10	..	42	..	21	..	13	..
Ireland								
Labour income	85	–1	48	2	64	1	86	6
Public social transfers	13	3	49	4	33	2	11	–4
Private transfers, capital, other income	2	–2	3	–5	3	–4	2	–3
Netherlands								
Labour income	85	2	38	1	58	–3	84	4
Public social transfers	13	–1	60	3	40	5	14	–2
Private transfers, capital, other income	2	–2	3	–3	2	–2	2	–2

a) Income concept used is disposable household income per equivalent person.

Source: Denmark: SFI database; Finland: IDS (Income Distribution Statistics); Ireland: national estimates based on ECHP (1995) and EU-SILC (2005); Netherlands: Secretariat estimates based on ECHP (1995) and EU-SILC (2005).

Among the population with disability, the "income package" differs significantly between those who have a job and those who do not. As a matter of fact, the income shares of employed persons with disability are almost identical to those of the population without disability, in all four countries, with earnings shares in total income of between 83% and 94%. This underlines the crucial importance of employment. While public policy often focuses on benefits, succeeding in increasing employment seems the best way to economic security for many people with a disability.

On the other hand, benefits and transfers constitute almost half of the disposable household income of non-employed persons with disability in Denmark and Ireland, and more than half in the Netherlands and Finland (if earnings-related pensions are counted with benefits). Given the sizeable share of public transfers and in particular disability benefits in the income package of people with disability, an important question concerns their redistributive features and the extent to which they provide income security for persons at the lower end of the distribution. Turning first to all public social transfers taken together (right-hand panel in Table 5.2), a little over one-third of those are going to the bottom quintile, while between 7% (Denmark) and 12% (Ireland, Netherlands) are accruing to the top quintile. This makes all three countries considerably more redistributive in terms of public transfers than other OECD countries: on average across 21 OECD countries, the share of transfers going to the bottom quintile is less than one and a half times the one going to the top quintile. It is around three times as high in Ireland and the Netherlands and almost five times as high in Denmark.

Table 5.2. **Disability benefits are more redistributive in Ireland than elsewhere**

Shares of disability benefits and total public social transfers going to lowest and highest income quintiles, 2000-2005[a]

		Disability benefit			All public social transfers		
		(1) Lowest quintile	(2) Highest quintile	(1)/(2)	(1) Lowest quintile	(2) Highest quintile	(1)/(2)
Denmark	2000	30	7	4.3	37	8	4.8
	2005	27	6	4.5	36	7	4.9
Ireland	2000	47	7	6.6	35	10	3.4
	2004	45	7	6.4	33	12	2.7
Netherlands	2000	30	10	3.0	37	9	4.0
	2004	27	12	2.3	35	12	3.0
OECD-21	Around 2000	27	16	1.7	30	17	1.8
	Around 2005	25	16	1.6	24	19	1.3

a) Income concept: disposable household income per equivalent person. Disability benefit includes all disability-related public transfers.

Source: Computations from OECD income distribution questionnaire.

In Denmark and the Netherlands (as well as on OECD average), this pattern is quite similar for disability benefits though they seem to have a slightly smaller redistributive impact than all benefits taken together. It is very different in Ireland where almost half of disability benefits accrue to the bottom quintile and the bottom-to-top ratio reaches 6.4. This is partly due to the fact that disability allowance (included in the figure) is means-tested and other disability payments are flat-rate. Except in Denmark, the redistributive impact of both disability benefits and all public transfers has become smaller over the past five years. That said, even if less progressively distributed, disability and other social benefits alleviate inequalities of other income sources, especially those of market incomes, in all countries.[3]

B. The tax/benefit position of persons with disability

The disability benefit and tax systems share some common features across the four countries but differ considerably in other aspects (see Annex Table 5.A1.1 and Box 2.1 in Chapter 2). This has to do with different social protection histories and traditions. Denmark is the only country with one single benefit for people with disability – a consequence of a reform in 2003 through which the hitherto complex benefit system was simplified considerably (Chapter 2). As is the case of all other social benefits in this country, it is financed through taxes and has universal coverage. In addition, persons with partial work capacity queuing for a flex-job are entitled to a waiting benefit, the payment rates of which are closely linked to unemployment benefit. Finland operates a dual system with a tax-financed and universal national disability pension and an earnings-related contribution-based statutory disability pension. The two schemes are integrated and counted against each other.[4] The universal schemes in the two Nordic countries (disability pension in Denmark and national pension in Finland) provide flat-rate benefits up to a certain income level (differentiated by household type).

Ireland operates two major disability-related benefits – invalidity pension which is contribution-based and covers employed people only, and a non-taxable means-tested benefit with universal coverage, disability allowance. Ireland also has an illness benefit which can be received without time limit.[5] The three schemes provide quite similar flat-rate benefit rates. The main scheme in the Netherlands, WIA (as well as the former WAO) is contribution-based and covers employees only. It consists of two provisions: a benefit for persons with at least 80% permanent disability (IVA) with rates related to past earnings up to a maximum; and a return-to-work benefit (WGA) for people with partial work capacity. This benefit is initially wage-related and, after some time, transforms into either a follow-up benefit (if the person is not working) or a wage supplement (if working "sufficiently"). The Netherlands also has a special and universal scheme for young people with disability, called Wajong. Among the four countries, Finland and the Netherlands operate genuine partial (and graduated) disability benefits, although the Danish flex-job scheme (which is available at two different capacity levels) serves a similar purpose.

Table 5.3 compares the tax/benefit position of a 40-year-old single person with average earnings when working and after going on full disability benefit. The first column for each country describes the steps from gross to net earnings for a working person. With 15%, the burden of taxation is considerably lower in Ireland than in the other three countries (between 30% in Finland and 40% in Denmark). The weight of social security contributions to total taxation is lowest in Denmark. In Finland and the Netherlands, they contribute about one-third to the total tax burden, an order of magnitude found in many Continental European countries. In the Netherlands, however, social security contributions are much more important than direct income taxes. In the two Nordic countries, especially in Finland, local income taxes play a more significant role than central government taxes.

The second column for each country in Table 5.3 looks at the tax/benefit position of a single person after having moved from work to a full disability benefit. The third and fourth columns show the position of a person who moved from work to other types of disability benefits. The tax weight on benefits is much lower than for workers, and zero in the case of disability allowance in Ireland due to non-taxation of benefits. *Gross* replacement rates, *i.e.* gross benefit levels with regard to former gross earnings, are therefore lower than *net* replacement rates. In all countries, tax credits are used to ease the tax burden of disability beneficiaries and they are particularly important in Ireland.

In Denmark, Finland and the Netherlands, full disability benefits replace about two-thirds or more of former earnings in the case of a single person who used to earn an average wage. With 72%, the net replacement rate is highest for a Dutch person on initial WGA benefit.[6] The rate is 69% for Finnish recipients of earnings-related disability pensions and 66% for a Danish disability pensioner. In Ireland, net replacement rates are considerably lower – 54 to 55% – and they are practically identical between the three different schemes. This is not the case in the Netherlands, where the follow-on benefit of the WGA disability payment provides a 16 percentage point lower rate than the initial payment. That said, the net replacement rate of the follow-on benefit is still in the order of the Irish full benefit replacement rates.

Also in terms of *absolute* levels of regular benefits, expressed in USD in purchasing power parities, these are lowest in Ireland (a little below USD 14 000), around USD 15 000 to 16 000 in the two Nordic countries, and highest in the Netherlands (close to USD 20 000).

C. Adequacy and generosity of replacement rates

Net replacement rates (NRRs) compare the income situation when moving from paid work to inactivity. They thus provide indicators of both the adequacy and generosity of disability benefit schemes. Low NRRs for people who become totally incapacitated for work in the midst of their professional career may raise concerns about poverty and social

Table 5.3. **Gross and net replacement rates for main disability schemes are lower in Ireland**

The tax/benefit position of a single person at average earnings and when out of work on disability benefits, USD Purchasing Power Parities (PPP), 2006[a]

		Denmark			Finland		Ireland				Netherlands		
		Working single person	Disability pension	Waiting benefit	Working single person	Disability pension	Working single person	Illness benefit	Invalidity pension	Disability allowance	Working single person	Full disability benefit (WGA)[b]	Follow-on benefit (WGA)[b]
A.1	**Gross earnings**	38 581			34 615		29 698				43 023		
A.2	**Taxable benefits**												
	Disability benefits		20 226	18 400		21 809		8 546	9 227			30 116	10 194
	Social assistance benefits[c]												3 283
	Total taxable benefits		20 226	18 400		21 809						30 116	13 477
B.	**Income tax and social security contributions**	0	0	0	0	0	0	0	0		0	0	0
	State taxable income (after allowances, deductions, credits)	33 425	20 226	18 286	32 019	21 809	29 698	8 546	9 227		43 846	31 343	10 857
	State income tax	2 204	1 108	1 002	3 107	1 116	5 940	1 709	1 845		5 983	1 665	266
	Local taxable income (after allowances, deductions, credits)	33 425	20 226	18 286	28 827	21 809							
	Local income tax	9 646	5 246	4 599	5 304	4 013							
	Tax credits	246	246	246	162	119	3 093	1 616	1 616		268	160	160
	Social security contributions	4 305		114	2 339	327	1 520				9 787	8 920	2 061
	Total income tax and social security contributions	15 909	6 108	5 469	10 588	5 337	4 367	93	230		15 502	10 426	2 168
C.	**Non-taxable benefits**												
	Disability benefits									8 943			
	Housing benefits	409	1 075	1 075				5 270	4 589	4 873			4 211
	Total non-taxable benefits	409	1 075	1 075				5 270	4 589	13 816			4 211
D.	**Net income out of work (A – B + C)**		15 192	14 006		16 472		13 722	13 586	13 816		19 690	15 521
E.	**Net income in work (A1-B)**	23 081			24 027		25 331				27 521		
F.	**Gross replacement rate [(A2 + C)/A1]**		**55%**	**50%**		**63%**		**47%**	**47%**	**47%**		**70%**	**41%**
G.	**Net replacement rate (D/E)**		**66%**	**61%**		**69%**		**54%**	**54%**	**55%**		**72%**	**56%**

a) Average earnings refer to average wage (AW): DKK 330 900 in Denmark, EUR 33 543 in Finland, EUR 38 491 in the Netherlands and to average production worker wage (APW) in Ireland where AW is not available: EUR 29 960. Estimates refer to a 40 year-old single person with an earnings history of 22 years at average earnings. Figures assume that there is no waiting period between employment and the benefit situation.
b) WGA: person assumed to have 79% work incapacity and to receive top-up social assistance payments.
c) Net rates.
Source: Special module of OECD tax/benefit model. Information provided by national authorities.

exclusion, especially if the persons have caring obligations towards children. However, a majority of persons with disability are not fully incapacitated for work but experience problems of staying in the labour market. In the case of NRRs approaching or exceeding 100%, such schemes may become an attractive alternative to employment (for both employees and employers looking to adjust workforce size without causing labour discontent). Indeed, past OECD work suggests a positive correlation between scores on a synthetic "benefit generosity indicator" and both beneficiary rates and disability benefit inflows (OECD, 2003).

Countries have different disability schemes in place. They can be differentiated by whether or not the work capacity loss or disability is permanent, such as illness benefit and invalidity pension in Ireland, or by degree of work incapacity, such as the waiting benefit in Denmark or WGA in the Netherlands. In addition, there are special schemes for persons not covered otherwise such as disability allowance in Ireland.[7] A first issue is how these disability schemes compare to each other in terms of replacing earned income. Figure 5.1 compares NRRs for a single person (results for other household types are shown in Annex Figure 5.A1.1).

How do the different disability schemes fare compared to each other?

In Denmark and the Netherlands, NRRs for single persons are higher for those who receive disability benefit and WGA than for those on waiting benefit and WGA follow-on benefit, respectively. That said, in Denmark the difference is not particularly pronounced (except for persons with low former earnings) and in the case of couples, NRRs for disability benefits and waiting benefits are practically identical. In the Netherlands, the estimates shown for WGA follow-on benefits assume that the person is not receiving any top-up social assistance payments and are therefore between 20 and 30 percentage points lower than the initial WGA benefit. In practice, many people on WGA follow-on benefit will apply for and receive such top-ups (to which they are entitled) and increase their NRRs to the levels of social assistance, *i.e.* identical to WGA for former earnings up to 60% of average wage and 15 to 20 percentage points lower for earnings higher than that. It should also be noted that differences in NRRs between regular and partial or short-term disability benefits have been reported to be higher (between 20 to 40 percentage points) in other OECD countries reviewed recently, Spain and the United Kingdom (OECD, 2007). In Ireland, the three different schemes (IB, IP and DA) provide almost identical NRRs.

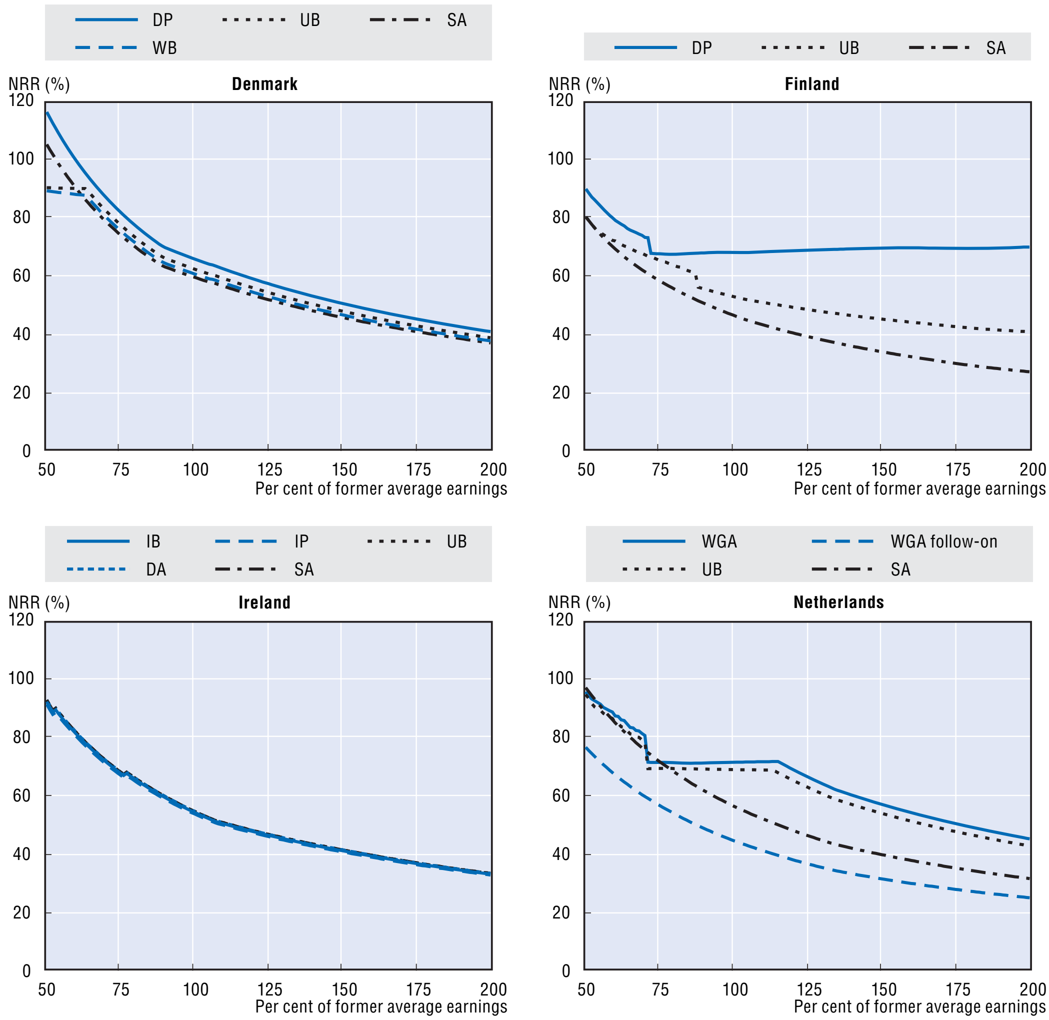
A second issue is how disability benefits compare, in terms of replacing earned income, with other main income support schemes for those of working-age: unemployment benefit and social assistance. In theory, these schemes have been distinct, serving different groups of people. However, there is some evidence that many persons with health problems – to which social and employment problems often are added – are being shifted around and, in the end, trapped between increasingly tightened schemes. Figure 5.1 also compares NRRs for disability, unemployment and social assistance benefit schemes.

How do main disability schemes compare with other benefit schemes for the working-age population?

In Denmark (except for former low wage earners), Ireland and the Netherlands, unemployment and disability benefits have almost identical replacement features throughout the whole earnings range considered (half to double the average wage). In many cases, NRRs for disability benefits are a few percentage points higher than for

Figure 5.1. **Disability and unemployment schemes provide similar net replacement incomes, except in Finland**

Net replacement rates for disability benefits, unemployment benefits and social assistance, single person 40 years old, 2006[a, b, c]



a) Net replacement rates (NRR): ratio of household net income after becoming inactive and receiving disability benefit or unemployment benefit or social assistance to household net income when earning 50% through 200% of average earnings. Estimates refer to a 40-year-old single person with a full earnings history since age 18.

b) DA = disability allowance; DP = disability pension; IB = illness benefit; IP = invalidity pension; SA = social assistance; UB = unemployment benefit; WB = waiting benefit; WGA = initial disability benefit in the Netherlands; WGA follow-on = subsequent disability benefit in the Netherlands.

c) WGA: person assumed to have 79% work incapacity, without receiving top-up social assistance payments.

Source: Special module of OECD tax/benefit model. Information provided by national authorities.

unemployed persons, and in a few cases, they are substantially higher: for former low-wage earners in Denmark (*i.e.* below approximately 60% of the average wage), and for two-earner couples with two children in the Netherlands. The pattern is quite different in Finland. There, NRRs for disability and unemployment benefits are quite similar only up to around a former earnings level of two-thirds the average wage – around 70%-80% for singles and one-earner couples and 90% for two-earner couples. Starting from two-thirds of average wage, NRRs for unemployment beneficiaries are gradually falling to 40% (in the case of single persons) but remain at a constant 70% for disability benefit recipients. This is due to the earnings-related nature of the disability benefit in Finland and the fact that there exists no maximum benefit.

Only in Finland and the Netherlands, both unemployment and disability benefits provide higher NRRs than regular social assistance, and even in these two countries this is not the case for former lower wage levels. In Denmark, NRRs for social assistance recipients are only marginally lower. In all four countries, NRRs for social assistance recipients tend to be lower, however, as soon as there is a second earner in the family.

NRR features for singles and one-earner couples in Ireland are unique as all working-age benefits – social assistance, unemployment benefit and the three disability benefits considered – provide almost identical NRRs. This is partly due to housing benefit top-ups which are paid throughout the whole earnings range. That said, estimates excluding housing costs also result in very similar NRRs across the schemes.

How does family structure affect benefit entitlements?

NRRs for disability benefits can be considerably higher when there are children present in the household. For instance, in the area around former average earnings, they are some 10-15 percentage points higher than for singles in all four countries. This is due to general child benefits and family allowances, but also to special child supplements within the disability benefit system as is the case in Finland and Ireland.

NRRs for disability benefits for inactive childless couples are quite similar to those for singles. The major exception is Ireland where NRRs are significantly higher for inactive couples than for singles throughout the whole earnings range. This is due to benefit supplements for dependent (*i.e.* inactive) spouses, on the one hand, and lower taxation on the other.

The interplay of different benefits, minima and maxima, income-test thresholds and taxation may cause several "spikes" in the NRRs for disability beneficiaries as former earnings increase. Withdrawal of means-tested benefits (social assistance payments, housing benefits) and differences in tax rules at specific income levels can drive NRRs up at some earnings levels and down at others. For example in Finland, "spikes" appear at around 70% of average earnings (for disability benefit) and 90% of average earnings (for unemployment benefits) when housing benefit entitlements stop.[8] This is also the reason for the sudden fall of NRRs for disability and unemployment benefits in the Netherlands, at around 70% average wage. The two smaller breaks in the Irish NRR lines are due to taxation for working people: until around half the average wage they do not pay income taxes, and until around three quarters of average wage, they do not pay health insurance contributions.

It should be noted that the model estimates presented here do not take into account a number of special and individualised monetary benefits and related or derived in-kind benefits. In Denmark this concerns, for instance, a cash benefit designed to compensate additional expenses on the grounds of specific handicaps (*merudgiftsydelse*). In Finland, there exist allowances for specific health conditions (*e.g.* nutrition grants) but also a special disability allowance for non-beneficiaries to compensate for hardship arising from illnesses. In Ireland, the receipt of disability payments is linked to access to a free medical card.[9] These transfers and services may increase the "net worth" of disability benefits for some recipients and are not reflected in the NRR figures above.

To sum up, income from work dominates the household income package of people with disabilities. For those who are inactive and on benefit, regulations on taxes and transfers determine net replacement rates. The latter tend to be lower in Ireland than in the other countries. Moreover, disability benefits generally provide net replacement income similar to unemployment benefits in Denmark, Ireland and the Netherlands and, except for former lower wage earners, considerably higher net replacement income in Finland. Except in Denmark, the redistributive impact of disability benefits has become considerably smaller over the past five years.

5.2. Work incentives and disincentives for disability benefit recipients

This section looks at *financial* work incentives and disincentives for persons with disability through the tax/benefit scheme. Non-financial incentives – *e.g.* stemming from eligibility and duration criteria for various benefits and programmes and the extent of follow-up and activation policies towards persons on such schemes – are discussed elsewhere in the review. Here, the net income effects of transitions into or within work are considered. That is, the transition from inactivity into work, *i.e.* the extent to which gains in earnings are "taxed away" through a combination of reduced benefits and higher taxes, when taking up work – expressed as average effective tax rates (AETR) – or when increasing hours of work – measured through marginal effective tax rates (METR).

A. Does it pay to work?

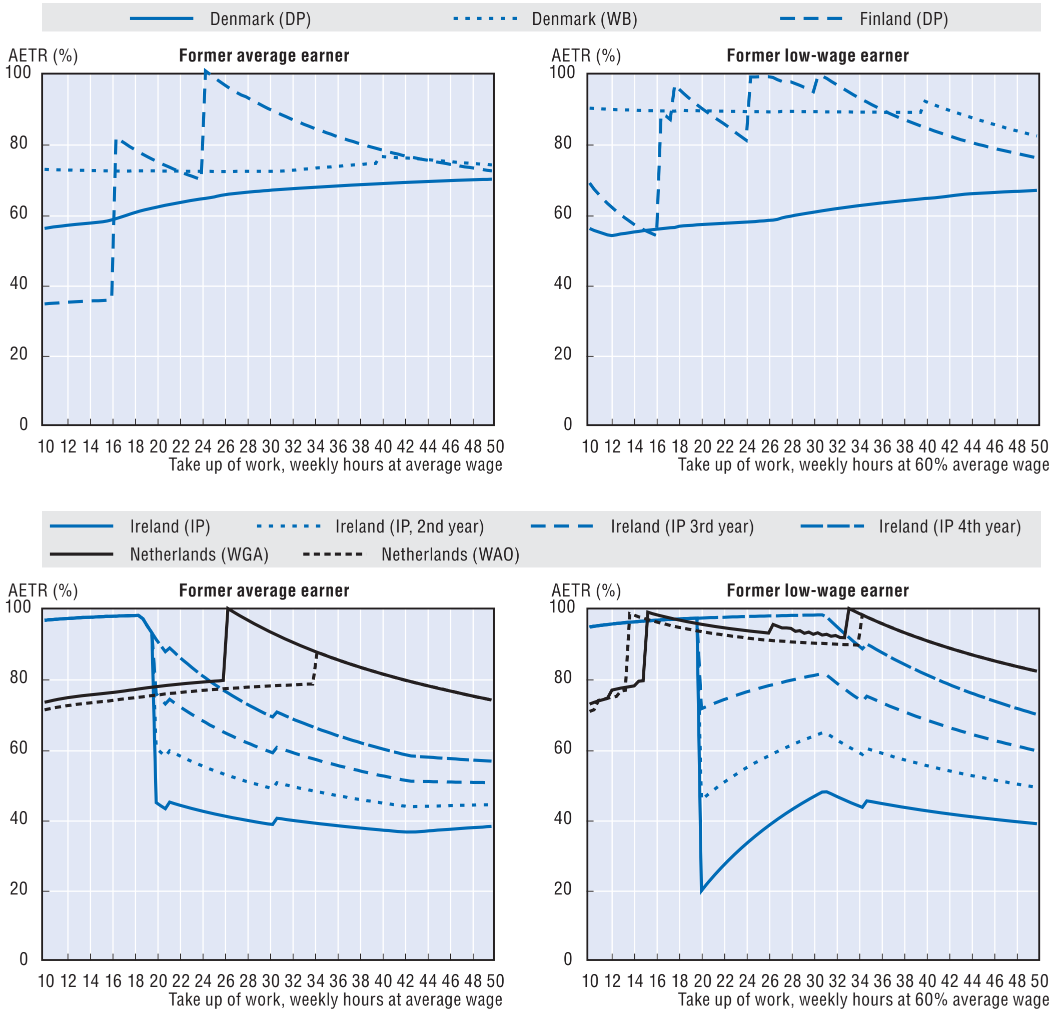
Once inactive and on disability benefit, what are the financial consequences of a return to work? This question will be particularly relevant for those people with remaining work capacities, in particular those on temporary or partial benefits. Partial benefits notably exist in Finland and the Netherlands, and the first set of considerations below is based on the realistic assumption that people on partial benefits are combining these with work.[10] Taking up work should be financially attractive for those considering this step. This is, however, not always the case. Figure 5.2 shows average effective tax rates embedded in the countries' main disability schemes, for single persons with two different earnings histories: those who were on average wage prior to acquiring a disability, and those who were on low wages.[11] It is assumed that persons return to a job at the same wage rate but for varying working hours up to the former wage level.[12] The following key findings emerge.

Denmark is the only country, in which effective taxation for disability beneficiaries is almost independent from the amount of work taken up: between six and seven Danish Crowns are "taxed away" for every ten Crowns earned (Figure 5.2). This is due to a smooth interplay between a gradual phase-out of disability benefit,[13] comprehensive taxation and top-up of housing benefits at a broader range of lower earnings levels (until about two-thirds of average earnings). At around 70-75%, average taxation for people on waiting benefits is slightly higher when they were average earners, but considerably higher when they were low-wage earners: close to 90%. This is due to the fact that waiting benefits are calculated according to unemployment benefits[14] and, for low-wage earners, they are tapered away by the same absolute but a higher relative size than for average earners. When taking up work at the former wage level, waiting benefits are suspended, creating a small increase in AETRs at the level of full-time work (40 hours).

Average taxation for disability beneficiaries in Finland is relatively low, some 30%, but only up to engaging in work for 16 hours (*i.e.* 40% of their former earnings level). At that

Figure 5.2. **Taking up work pays in Denmark and especially Ireland**

Average effective tax rates for a 40-year-old single person with disability, 2006[a, b]



a) Average effective tax rate (AETR) is the percentage of earnings that is taxed away via increased taxes and reduced benefits when taking up work. Take-up of work at 10 and 50 hours weekly work, at average wage AW (Panel A) or low wage (Panel B). The person is assumed to be on disability benefit after having worked at 100% of AW (Panel A) or at low wage (Panel B). Irish data where AW estimates are not available are based on average production worker wage APW. Low wages defined as 60% of AW/APW. Estimates refer to a 40-year-old person with a full earnings history since age 18.

b) DP = disability pension; IP = invalidity pension; WAO = former disability benefit in the Netherlands; WB = waiting benefit; WGA = current disability benefit in the Netherlands.

Source: Special module of OECD tax/benefit model. Information provided by national authorities.

stage, the full disability benefit is transformed into a partial one and the AETR doubles to some 80%[15] (Figure 5.2). A second such jump in AETR arises when the person works more than 24 hours (60%) as they then lose benefit entitlement altogether. At that stage, work does not pay at all and the AETR returns only to 80% when taking up a full-time job. For former low-wage earners, even working for less than 16 hours is somewhat less attractive than for average earners. This has to do with a *relatively* higher starting level of net income when out of work due, *inter alia*, to housing benefits.

Finland operates an employment-conditional benefit in the form of an "earned income allowance". While this benefit is available to all persons taking up work, there is also a special tax allowance and a tax credit targeted for persons with disabilities in Finland. Nonetheless, these instruments impede only very little if at all on effective taxation, hence, incentives to work. In-work benefits, for instance, constitute just some 3-4% of net income for both former average and low-income earners should they take up work for 16 hours.

In contrast, in-work benefits seem to have more potential in Ireland. Recipients of working-age benefits, including all disability-related payments are entitled to a Back-to-Work Allowance (BTWA) should they take up work for at least 20 hours. This causes the AETR to drop from a level close to 100% to some 45% for former average earners and a low 20% for low-wage earners, at take up of half-time work (Figure 5.2). AETRs for average earners then decrease further except for two small increases when income taxation and health insurance contributions set in, respectively. Effective taxation is 40% when taking up full-time work. On the other hand, AETRs for low-wage earners increase in the band of 20 to 32 hours of work, mainly because of housing benefits being phased out. The AETR is 43% when they take up full-time work.

However, to the difference of the Finish in-work benefits, the Irish Back-to-Work Allowance is limited in time and phased out rather substantially. It entitles to 75% of the former benefit in the first year, 50% in the second and 25% in the third year. Figure 5.2 also shows that this phase out leads to 10 percentage point increases in AETRs per year for former average earners. After the third year, they face a 60% AETR when taking up full-time work. The situation is worse for former low-age earners. The yearly increase in AETRs is much more pronounced, and after the third year, a former low-wage earner faces AETRs between 80% and 100% when taking up part-time or full-time work. This time limitation and phase-out may therefore explain the low take-up of these in-work benefits in Ireland: less than 1% of all recipients of disability payments make use of the BTWA.

In the Netherlands, effective taxation is high. People on initial WGA benefit considering to take up work will see EUR 7 to 8 being taxed away for every EUR 10 gain in gross earnings. Above 65% of former earnings (corresponding to 26 hours of work), persons will lose their WGA benefit and AETRs reach a level of 100%. At full-time work, the level is still around 80%. Compared to the former WAO initial benefit, AETRs are similarly high with the only exception that the jump in AETR levels for WAO occurs later, namely at 85% of former earnings (34 hours of work). This is linked to the change in the minimum threshold for benefit recipiency, from 15% (WAO) to 35% (WGA). For former low-wage earners peaks in AETRs occur already earlier, at around 14 to 15 hours. This is due to the suspension of housing benefits at these earnings levels. When out of work, these constitute some 18% of net income of disability beneficiaries.[16]

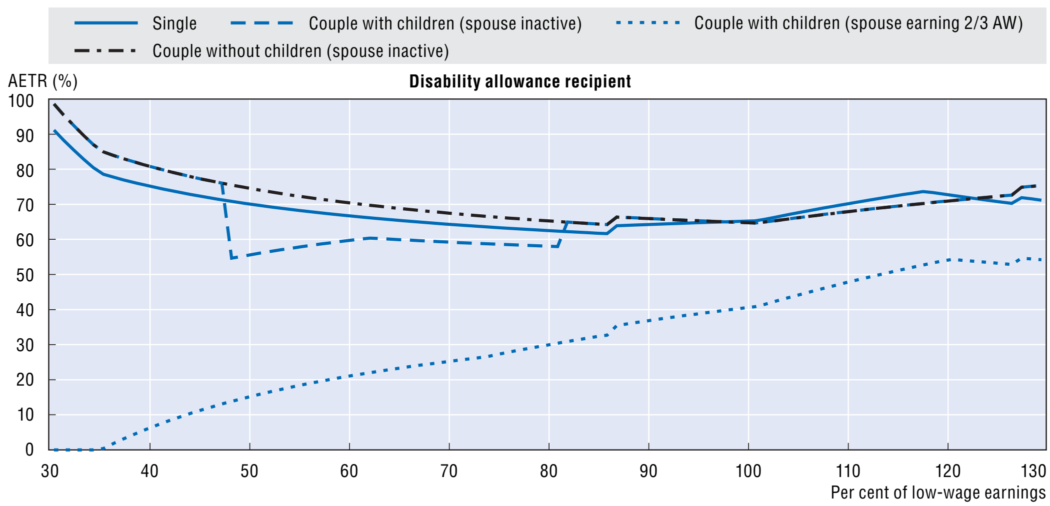
Household composition can influence financial work incentives for disability beneficiaries, especially in case of withdrawal of child or family-related benefits, or different earnings disregards depending on the activity of the partner. This issue plays a significant role only in Ireland. In the other three countries, AETRs for different household constellations are practically identical, with the exception of single parents, who face slightly higher AETRs in the two Nordic countries and slightly lower ones in the Netherlands.

In Ireland, to the contrary, AETRs are generally lower for persons with disability who live in households with children, in the area between half-time and full-time work. This is partly due to the Family Income Supplement (FIS), operated in this country. FIS is an employment-conditional benefit for parents working at least 19 hours per week[17] which pays 60% of the difference between the net family income and a specified earnings limit, with a minimum supplement of EUR 20 per week. The earnings limit varies with the number of children and ranges from EUR 465 to 905; hence, FIS is focused at low-wage earners. The FIS take-up rate is estimated to be as low as 30-40%, but the payment has the potential to play a much greater role in making work pay and raising family income: it has been estimated that achieving a full take-up of FIS would lead to a 3 percentage point reduction in the key at-risk-of-poverty indicator (Callan *et al.*, 2006).

For instance, when taking up half-time work at low wages, AETRs for disability allowance (DA) recipients with an inactive spouse and two children fall by 20 percentage points from about 75% to 55% (Figure 5.3). AETRs remain on a lower level for these one-earner couples until FIS is phased out, at around the level of four days work per week. Note that AETRs for DA recipients with children whose partners are working (at two-thirds of the average wage in this case) are also very low and, indeed, below 40% up to full-time work. This is not due to FIS but to the fact that the *initial* disability allowance is significantly lower for these families because they do not receive (inactive) spouses supplement or housing benefit; two-earner couples have therefore less to lose' when taking up work. Both family types with children benefit from the DA earnings disregard but this is counted against housing benefits and spouse supplement in the case of one-earner couples. Nevertheless, the design of FIS could serve as a model for in-work benefits to improve work incentives for single persons with disability in the lower earnings range, not only for Ireland.

Figure 5.3. **Irish low-wage families with children have stronger incentives to work**

Average effective tax rates for a 40-year-old single person with disability, former low-wage earner, 2006[a]



a) Average effective tax rate (AETR) is the percentage of earnings that is taxed away via increased taxes and reduced benefits when taking up work. Take-up of work at between 30 and 130% of low wage, with the latter defined as 60% of APW. Estimates refer to a 40-year-old person with a full low-wage earnings history since age 18. Children are aged 4 and 6.

Source: Special module of OECD tax/benefit model. Information provided by national authorities.

B. Mobilising remaining work capacities

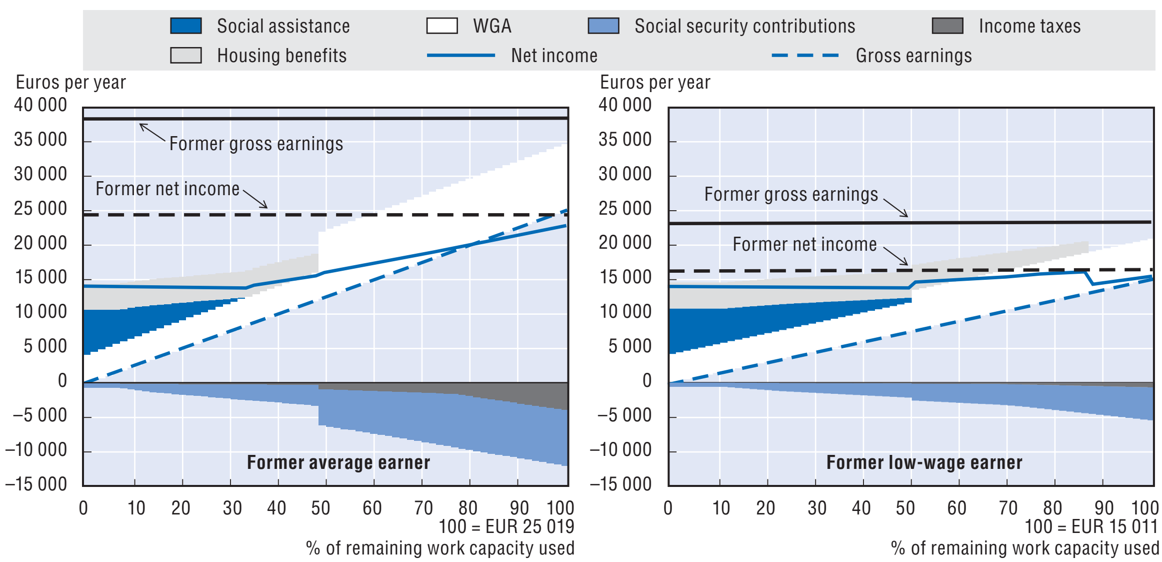
The considerations above refer to people on a full disability benefit who consider taking up work, at different working hours, corresponding to earnings levels between 25% and 125% of their former earnings. This implies that, when taking up work at a more substantive range, their disability benefits will be transformed into partial benefits (Finland, Netherlands), phased out (Denmark), or suspended (Ireland). It is thus assumed that persons who increase their earnings capacity correspondingly decrease their disability degree. Another relevant issue concerns persons on partial disability benefits with a fixed disability degree who consider making use of part or all of their remaining work capacities.

This question is particularly relevant in the Netherlands which introduced a new system of wage supplements to encourage people with partial earnings capacity loss to take up work in the limits of their remaining work capacity. Once the initial WGA benefit is exhausted,[18] the person is entitled to either a (lower) follow-on benefit or a wage supplement in case she is working at least at half of her residual earnings capacity. Figure 5.4 shows an example for a single person with a remaining work capacity of 65% – the new threshold for entering the WGA system – and two different earnings histories: average and low-wage earnings before disability occurred. The full residual earnings capacity therefore is EUR 25 000 in the first case and EUR 15 000 in the second. The horizontal axis denotes the percentage of capacity being used: from 50% remaining capacity being used, the WGA follow-on benefit is being replaced by the more generous WGA wage supplement. If the person were to use more than 100% of her remaining capacity, all WGA payments would be suspended.

Figure 5.4 shows that the WGA wage supplement helps making work pay although the interplay with income taxes and other benefits considerably attenuates the role of these

Figure 5.4. **The Dutch WGA wage supplement provides weaker work incentives for former low-wage earners**

Gross and net income of a single person with 65% remaining work capacity, by percentage of work capacity used, Netherlands, 2006[a]



WGA = Follow-on disability benefit or wage supplement.

a) Low wages defined as 60% of AW.

Source: Special module of OECD tax/benefit model. Information provided by national authorities.

supplements, especially for lower-wage earners. For a former average earner with 65% remaining work capacity, using at least half of the remaining capacity would provide a net replacement income of between 65% and 90% (if using her entire remaining capacity). If not working or using less than half of her capacity, the replacement rate is somewhat but not substantially lower, 56-60%. This is due to top-ups of housing benefit and social assistance at the bottom of the income ladder and higher income taxes and contributions at the upper part. The important role of housing benefit becomes clear when considering a former low-wage earner. In that case, the replacement rate would increase only slightly (from 85 to 90% and more) when using more than half of the remaining work capacity and there would even be a temporary decrease in the earnings range when housing benefit gets suspended.

That said, the important feature of the new measure is that it helps to avoid that additional Euros earned lead to only marginal increases, or even reductions, in net income because of loss of disability benefit, at least for average earners. Ways need to be found that the effectiveness of WGA wage supplements do not remain restricted to the mid-income range and, indeed, higher than average earners up to the maximum daily wage which is the cap for this supplement (around 120% of average wage).

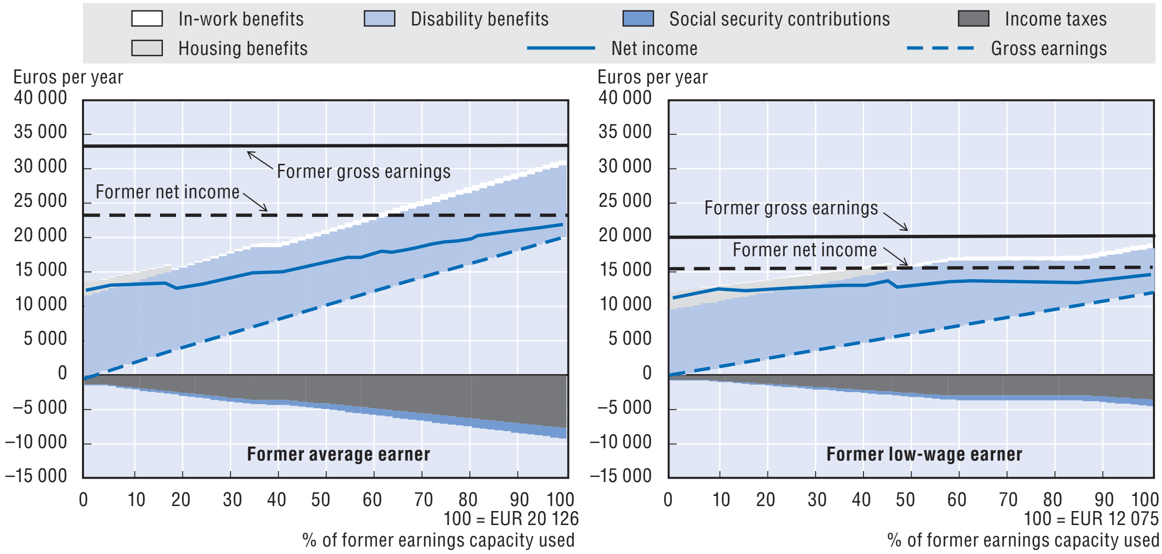
The situation is somewhat similar for Finnish partial disability beneficiaries although benefit regulations are different. The threshold for a partial benefit is 60% of remaining work capacity. National and earnings-related pensions are combined and the amount of the national pension is reduced by 50% of the earnings-related pension. When taking up work, the earnings-related pension part is paid independent of the amount worked (up to reaching full capacity level). On the other hand, the national pension part is counted against earnings but with an annual earnings disregard of EUR 7 064.

Figure 5.5 shows that for a former average earner on partial disability benefit, the net replacement rate is about 50% and for a former low-wage earner it is 70%. In both cases, these rates increase up to 95% when making use of the full remaining work capacity. Again, housing benefits play an important role in the lower income part and even causing a slight fall in net income at around 18% (average earner) and 45% (low-wage earner) of remaining work capacity. Between 38 and 42% of remaining capacity (average earner) and 60 and 88% (low-wage earner), the net income function becomes flat (*i.e.* additional gross earnings would not increase net income), as the earnings disregard for national pension is phased out at the first point and the national pension part in the second. Ways should be found to reward increasing work effort in these areas by giving, for instance, a greater role to (existing) in-work benefits.

The situation is different in Ireland. In this country, no partial disability scheme exists. However, in order to mobilise remaining partial work capacities, earnings disregards for disability allowance recipients who take up rehabilitative employment have been introduced recently. Recipients can work and have the first EUR 120 earnings per week disregarded entirely, plus 50% of earnings between EUR 120 and EUR 350.[19] Figure 5.6 shows that this disregard can be very effective: AETRs for former average earners now are significantly lower, up to 28 hours of weekly work. The effects are even more pronounced for former low-wage earners: without disregards, AETRs were 100% up to half-time work and beyond, but now they are in the range of 60-80%. This may explain the relative success of this measure: about 10% of disability allowance recipients availed of earnings disregards for rehabilitative work in 2007.

Figure 5.5. **High earnings disregards in the Finnish partial disability benefit, especially for former average earners**

Gross and net income of a single person with 60% remaining work capacity, by percentage of work capacity used, Finland, 2006[a]

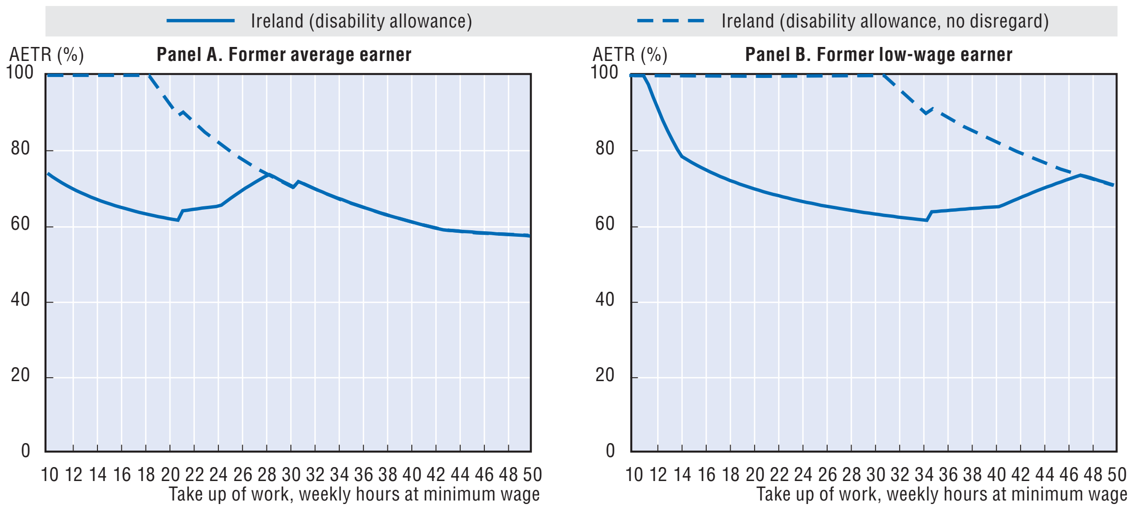


a) Low wages defined as 60% of AW.

Source: Special module of OECD tax/benefit model. Information provided by national authorities.

Figure 5.6. **The disability allowance earnings disregard in Ireland can be very effective, especially for low-wage earners**

Average effective tax rates for a 40-year-old single person in receipt of disability allowance, 2005[a]



a) Average effective tax rate (AETR) is the percentage of earnings that is taxed away via increased taxes and reduced benefits when taking up work. Take-up of work at 1 and 50 hours weekly work, at average wage (Panel A) or low wage (Panel B). The person is assumed to be on disability benefit after having worked at 100% of AW (Panel A) or at low wage (Panel B). Irish data where AW estimates are not available are based on average production worker wage APW. Low wages defined as 60% of AW/APW. Estimates refer to a 40-year-old person with a full earnings history since age 18.

Source: Special module of OECD tax/benefit model. Information provided by national authorities.

C. The impact of increasing work efforts

The discussion above has focused on *inactive* disability benefit recipients and the consequences when taking up work. A different yet important question arises for those persons who are *in* work already, possibly drawing a (partial) disability benefit, and considering to work more hours. Table 5.4 shows the financial consequences of increasing working hours for a person with disability, in four steps: from 0 to 10 hours (marginal work), from 10 to 20 hours (part-time), from 20 to 30 hours (considerable part-time) and from 30 to 40 hours (full-time). Again, two cases are considered: the person is assumed to have worked at average or low-wage earnings before the onset of disability and again to be taking up work at this hourly earnings level and receiving a partial disability benefit, if eligible.

First, there are several "zones" where working more hardly pays, *i.e.* with marginal effective tax rates close to or over 100%. In such cases, persons are encouraged to stay in their current benefit position despite their wish to become more active due to, for instance, improvements in their health condition. Such "zones" often occur when a disability benefit is suspended – taking account of other benefit reductions and taxation. Only in Denmark there are no such specific "zones" and METRs are constantly between 56 and 76% because a (gradually decreasing) disability benefit is paid throughout the whole earnings range.

Second, increasing working hours does in general not seem to be more attractive – in that less of additional earnings are "taxed away" – for low-wage than average wage earners. Low-wage earners may even face much higher METRs, especially in cases when increasing working hours lead to a loss of other social benefits, such as housing benefit. This is, for instance, the case in Ireland when changing from part-time to considerable part-time work and in the Netherlands for changes from marginal to part-time work and, for average earners, from part-time to considerable part-time work.

Third, in Finland and, to a lesser degree in Denmark and the Netherlands, engaging in little work entails comparatively lower METRs than increasing the number of hours worked, hence the issue seems to be one of a low-wage (poverty) trap more than of an

Table 5.4. **Increasing working hours may penalise workers with disability**

Marginal effective tax rates for those receiving full or partial disability benefits, percentage of earnings, 2006[a]

		Increase in working time			
		0 >>> 10 hours	10 >>> 20 hours	20 >>> 30 hours	30 >>> 40 hours
Denmark (DP)	Average earner	56	68	76	75
	Low-wage earner	56	58	68	76
Finland (DP)	Average earner	34	116	*120*	*43*
	Low-wage earner	69	111	*104*	*54*
Ireland (IP)	Average earner	*97*	*–7*	*27*	*32*
	Low-wage earner	*95*	*–55*	*100*	*31*
Netherlands (WGA)	Average earner	74	82	*126*	*46*
	Low-wage earner	73	118	*87*	*86*

DP = disability pension; IP = invalidity pension; WGA = initial disability benefit.

a) Average earnings refer to average wage (AW), except for Ireland where they refer to average production worker wage (APW). Low wages defined as 60% of AW/APW. Marginal effective tax rate (METR) is the percentage of earnings that is taxed away via increased taxes and reduced benefits when increasing working hours. The hourly wage is at the AW level (first line) or national low-wage wage level (second line). The person is assumed to be on full or partial disability benefit, provided such benefit exists. Ireland: persons on IP are assumed to be entitled to Back-To-Work-Allowance (1st year). Estimates refer to a 40-year-old single person with an earnings history of 22 years at AW respectively low-wage earnings. Figures in italics refer to situations where no more disability benefits are granted.

Source: Special module of OECD tax/benefit model. Information provided by national authorities.

inactivity trap. In Ireland, however, it is the opposite. For people on either invalidity pension or illness benefit, it does not pay to take up work for one or two days a week because disability payments are suspended and the Back-to-Work Allowance is not available at this earnings range. In turn, when out of work, net income is toped up considerably with housing benefits (about one-third of net income). However, at exactly half-time work take-up, METRs are slightly negative for average earners and considerably negative for low-wage earners establishing a huge incentive to take up work at this level. This effect flattens out over the years when BTWA is gradually reduced, or phased-out: METRs for low-wage earners are slightly negative after two years, some 45% after three years and close to 100% when they are no longer eligible for this in-work benefit.

5.3. Conclusion

Taxes and benefits determine the adequacy of public net transfers provided to people with disability but also the financial awards for those who take up work, in particular those with partial work capacity. Across full disability regimes, net replacement rates are lower in Ireland than in the other three countries: for single former average earners, they amount to some 55% in Ireland and to some 70% in Denmark, Finland and the Netherlands.

Ireland has the most fragmented system of disability-related benefits in operation. Nevertheless, judged in terms of outcomes, despite different benefit rates and taxation, net replacement rates of illness benefit, invalidity pension and disability allowance are identical, throughout the whole earnings range and across different household types. This suggests that there is room for unifying some of these payments.

In the short run, *i.e.* upon leaving the labour market, regular disability benefits appear to be more "attractive" than unemployment benefits only in Finland (except for the lower income range). In the other countries, they provide net replacement rates slightly below those of unemployment benefits. However, disability benefits are expected to provide a much more "permanent" source of replacement income than unemployment benefits.

The step to paid work can be costly for a person with disability ("inactivity trap"), as can be the decision to increase working hours or earnings ("low-wage trap"). The level of average effective taxation is indeed high in the four countries and can reach 70 to 90% for both average and low-wage earners. In Denmark, average effective tax rates are somewhat lower, especially for low-wage earners and more constant along the earnings range – but they still exceed 50%. Only Finnish disability beneficiaries who take up work for less than two days per week and Irish disability payment recipients who take up work for at least 20 hours will be able to keep more than half of their additional gross earnings.

In-work benefits exist in Finland and Ireland but are much more important in size in the latter country. Nevertheless, there seems to be a take-up problem, perhaps related to the temporary nature of BTWA in Ireland. Another employment-conditional benefit for families with children, the Family Income Supplement, has a considerable potential, too.

Earnings disregards are another inroad for boosting work incentives, especially among people with partial work capacities. The new wage-supplement for people with partial work capacity in the Netherlands seems to be an effective tool, but only for former average-wage earners. In Finland, earnings disregards ensure that net replacement rates increase considerably when people make use of their full remaining work capacity but less so when working less. In Ireland, a recently introduced earnings disregard for DA recipients lowers effective tax rates, especially among low-wage earners.

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Notes

1. For Finland, trend data are only available for the more restrictive definition of "administrative" disability status, *i.e.* for persons who are eligible for tax allowances due to a disability degree of between 30% and 100%. These data suggest that the labour income share has increased by 4 percentage points during the past ten years for people with disability and by 6 percentage points for people without disability.
2. If one assumes a similar share of capital income in Finland as in the other countries, the transfer share in Finland would be similar to the one in Ireland.
3. This refers to the overall impact of these benefits among the total working-age population in 2000 (Förster and Mira d'Ercole, 2005).
4. In 2006, about 40% of all disability beneficiaries combined both types of payments. This share was more than double prior to 1996 when the national disability pension became fully pension-income tested.
5. Throughout this report, this scheme is classified as a sickness benefit in the first two years of benefit receipt, and as another disability benefit after these two years.
6. The initial WGA benefit provides the same replacement income as the full disability benefit for fully and permanently incapacitated persons (IVA).
7. The national pension in Finland has the same role. Currently, about 20% of Finnish disability beneficiaries receive a national pension only.
8. There are no such spikes in the case of two-earner couples since these families are not eligible for housing benefits throughout the whole earnings range.
9. Under the medical card assessment guidelines, persons whose weekly incomes are derived solely from DSFA or HSE payments, even if these exceed the stated threshold, qualify for a medical card.
10. This also implies that persons taking up work beyond the minimum threshold for claiming disability benefits (*e.g.* 35% in the Netherlands, or 40% in Finland) are assumed to lose these benefits.
11. Low wages are defined as 60% of average wage in each country. This comes quite close to the level of the minimum wage in Ireland, and the higher sectoral minimum wage rates applied in Denmark and Finland. The minimum wage level in the Netherlands is lower, about 40% of average earnings.
12. Above that level, it is assumed that people receive higher wage rates.
13. In the case of a single former average earner, the disability pension is completely phased out only at 1.9 times average earnings.
14. It should be noted that both disability beneficiaries and people on waiting benefit face lower effective taxation than unemployment beneficiaries in Denmark.
15. The model assumes identity between 40% of full-time hours and 40% of earnings – the threshold for partial disability benefit in Finland.
16. Housing benefits may indeed influence the interpretation of results. The OECD models assume that the person is eligible for housing benefit and that the costs for rent amount to 20% of average earnings. Alternative calculations assuming no housing benefit entitlements show that AETRs would be slightly lower for the Netherlands (2 to 5 percentage points), but 10 to 20 percentage points lower in Ireland. On the other hand, this would have no effect on indicators in Denmark and Finland.
17. Married or cohabiting couples can add their hours together.
18. This depends on the individual's employment record and varies between 6 and 60 months. In the example of the OECD model, the WGA duration would be two years.
19. The disregard applies to rehabilitative work only, as certified by medical evidence from the treating doctor.

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ANNEX 5.A1

Background Tables for Different Household Types

Income positions when persons are in work and when they are out of work are strongly influenced by the level and design of taxation and available benefits and their interaction with personal and household incomes. The analysis in Chapter 5 is based on estimations from an additional module to the OECD tax/benefit model (OECD, 2007b), for different groups of people with disability: those living alone, those living with inactive spouses and those living with working spouses (with and without children for all three constellations).

Table 5.A1.1 summarises the main features of the four countries' disability benefit systems, their taxation and the rules for combining benefits with labour earnings.* Figure 5.A1.1 complements the results for single persons shown in Figure 5.1, with estimates on net replacement rates for disability benefits, unemployment benefits and social assistance for two other household types: a person with disability living with an inactive spouse and one living with a spouse earning two-thirds of an average wage (in both cases having two children).

* A detailed description of the country-specific parameters of the disability systems that have been used for the models is available at *www.oecd.org/els/disability*.

Table 5.A1.1. **Main characteristics of disability benefit and taxation systems, as at 1 July 2006**

	DENMARK	FINLAND	IRELAND	NETHERLANDS
Benefit schemes (covered in model)	1. Disability pension (*Førtidspension*). Tax financed universal protection scheme for all inhabitants. 2. Waiting allowance (*Ledighedsydelse*): allowance for people waiting on flex-job.	1. Statutory earnings-related pension (*Työeläke*): contribution based, covering all economically active persons (employees, self-employed, farmers). 2. National pension (*Kansaneläke*): universal coverage guaranteeing a minimum pension.	1. Invalidity pension (IP). Social insurance scheme financed by contributions for employees with flat-rate benefits. 2. Disability allowance (DA). Universal scheme for persons substantially handicapped in undertaking work of a kind which, if not suffering from that disability, would be suited to age, experience and qualifications. 3. Illness benefit (IB, formerly Disability benefit, DB).	1. Before 2006: WAO (*Wet op de ArbeidsongeschiktheidsverzekEring*): employees with at least 15% earnings incapacity. Since 2006: WIA (*Wet Werk en Inkomen naar Arbeidsvermogen*): employees with at least 35% earnings incapacity, consists of two parts: WGA, IVA. 2. WGA (*Regeling Werkhervatting Gedeeltelijk Arbeidsgehandicapten*): persons with temporary or partial disability, transforming after some time into follow-up benefit (if not sufficiently working) or wage supplement (if sufficiently working). 3. IVA (*Regeling Inkomensvoorziening Volledig Arbeidsongeschikten*): persons with permanent and full disability (80%).
Benefit formula	1. Disability pension: up to certain income level, DKK 177 636 (EUR 23 823)/year for persons living alone and DKK 150 984 (EUR 20 248) for married or co-habiting pensioners.	1. Statutory earnings-related pension: accrued pension amount increased with accrual for projected pensionable service up to retirement age (minimum earnings EUR 13 358.40 during 10 years preceding the contingency). Accrual rate on annual earnings: 1.5% between age 18-52, 1.9% between age 53-62 and 4.5% between age 63-68. Accrual rates for projected service: 1.5% until age 50 and 1.3% between ages 50-63. Calculation basis: earnings during the five years preceding the contingency. For pensioners who are in employment, accrual rate is 1.5% of earnings. Accrual rate for unpaid periods 1.5%.	1. IP: Flat-rate amounts depending on age. • EUR 171.30 per week, if aged under 65. • EUR 193.30 per week if aged between 65 and 80 years. • EUR 203.30 per week if recipient is aged 80 or over.	1. WAO (before 2006): • Initial benefit: daily allowance between 14% and 70% of the daily wage (pre-disability wage up to maximum daily wage) depending on the incapacity level. Ceiling: EUR 170.33/day. • Continuing benefit: for each year above age 15, 2% of the difference between the previous wage (maximum EUR 170.33/day) and the minimum wage is added to this minimum wage.

Table 5.A1.1. **Main characteristics of disability benefit and taxation systems, as at 1 July 2006** *(cont.)*

	DENMARK	FINLAND	IRELAND	NETHERLANDS
	2. Waiting allowance: between 91% and 82% of the highest unemployment benefit, *i.e.* DKK 3 035 and DKK 2 735/week. Ceiling: average individual income during past 12 months.	2. National pension: full amount between EUR 432.44 and EUR 510.80 according to marital status and municipality. A full pension if resident of Finland, 80% of time after age 16 and before pension starts. Otherwise pension is adjusted to the length of residence. Reduced by 50% of the amount of the Statutory earnings-related pension and other Finnish and foreign pensions when annual total exceeds EUR 567.	2. DA: • Personal rate: EUR 165.80 per week. 3. IB: • Personal rate: EUR 165.80 per week.	2. WGA (since 2006): • Initial benefit: 70% of the (maximum) daily wage (pre-disability wage up to the maximum daily wage) if not working and 70% of the difference between the (maximum) daily wage and the individual's work-related income if working. • WGA follow-on benefit: 70% of the statutory minimum wage multiplied by the percentage of incapacity. If monthly wage is less than the statutory minimum wage, WGA follow-on benefit will be 70% of the daily wage, multiplied by the percentage of incapacity. • Wage supplement: 70% of the difference between the (maximum) daily wage and assessed residual capacity (pre-disability wage multiplied by percentage of incapacity). Wage-related WGA benefit may not be less than the level of the WGA follow-on benefit. 3. IVA (since 2006): 70% of the last earned wage. Ceiling: EUR 170.33 per day.
Minima/maxima	– Minimum pension: 1/40 of the above mentioned amounts. – Maximum pension: full rate (40/40) of the above mentioned amounts.	No minima, no maxima.	IB: minimum amount is EUR 74.50 per week when weekly earnings are below EUR 80.	WIA/WAO: No minimum benefits. Maxima: see above.
Special supplements (covered)	No supplements for dependants.	Children: National pension (*Kansaneläke*): Child increase EUR 18.68 per month and child under the age of 16.	1. IP: supplements for dependants. Spouse aged under 66 years: EUR 122.20 per week, aged 66 years and over: EUR 149.30 per week. For each child: EUR 19.30 per week. 2. DA: increase for a qualified adult: EUR 110.00; Increase for each qualified child: EUR 16.80. Where a claimant's spouse or partner is not a qualified adult, increases in respect of qualified children are generally payable at half-rate, depending on the exact circumstances. 3. IB: increase for a qualified adult: EUR 110.00; increase for each qualified child: EUR 16.80. An additional allowance of EUR 7.70 is payable to recipients of IP and DA who are living alone.	No supplements for dependants.

Table 5.A1.1. **Main characteristics of disability benefit and taxation systems, as at 1 July 2006** *(cont.)*

	DENMARK	FINLAND	IRELAND	NETHERLANDS
Graduation of benefits	No	Yes, for earnings-related pension: partial disability pension (*Osatyökyvyttömyyseläke*): 50% of the full disability pension.	No	Yes
Benefit schemes (not covered)	Cash benefit to compensate additional expenses on the grounds of the handicap (*Merudgiftsydelse*). The amount is fixed for each individual case, taking into account the expenses to be expected. Minimum DKK 6 000 (EUR 805) per year.	• Pensioners & acute care allowance (*Eläkkeensaajien Hoitotuki*): Payable to compensate for costs arising from home care or other special expenses caused by illness or injury. • Pensioners & acute housing allowance (*Eläkkeensaajien Asumistuki*). • Disability allowance (*Vammaistuki*) for non-pensioners: for 16-64 year old persons who are not in receipt of a pension but whose healthis weakened through illness or injury to compensate for hardship, necessary services etc. • Dietary grant EUR 21 per month, compensates celiacs for some of the additional cost of gluten-free nutrition. • Cash rehabilitation benefit/subsidy = time-limited disability pension (*Kuntoutustuki*) or rehabilitation allowance (*Kuntoutusraha*).	• Free travel. recipients may also qualify for fuel allowance, electricity allowance, T.V. licence and telephone rental allowance. • Carer's allowance (since 1990), carer's benefit scheme (since 2000), people caring on a fulltime basis for invalidity pensioners.	Wajong (*Wet Arbeidsongeschiktheidsvoorziening Jonggehandicapten*), Disablement Assistance for Handicapped Young Persons. The basis for this benefit is the statutory gross minimum (youth) wage per month excluding holiday allowance, divided by 21.

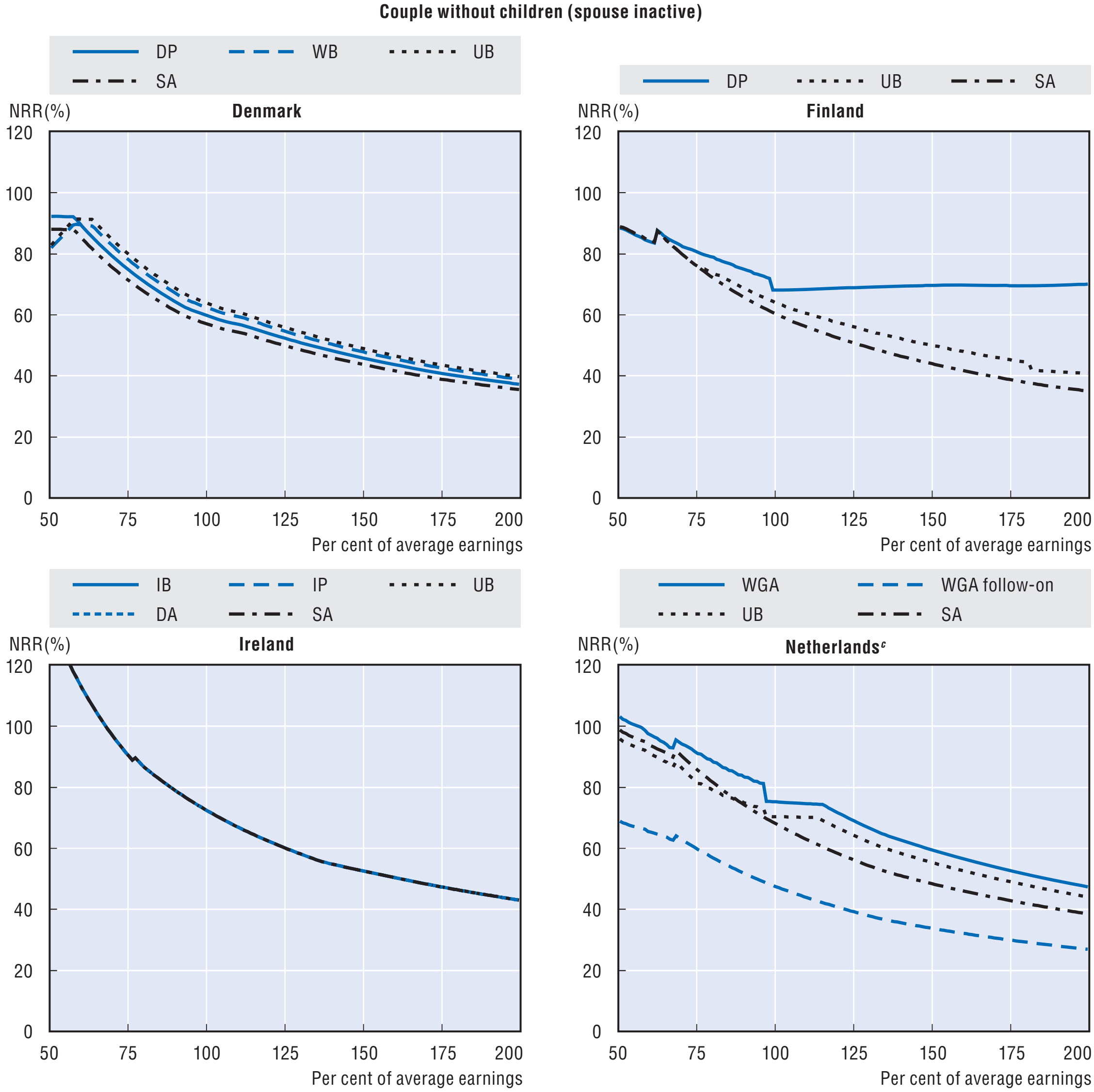
Taxation of benefits	Pensions are subject to taxation. General taxation rules. No special relief for pensions.	Pensions taxed as other earnings. Small pensions are entitled to a special pension deduction. If the income consists of national pension only, no income tax is paid. Disability allowance, Pensioners & acute care allowance and Pensioners & acute housing allowance are not taxed. Amounts of full pension deduction for pension income/year:
		• Local taxes: Single person EUR 6 950; married person EUR 5 960.
		• Government taxes: EUR 1 460 for all. When pension is higher than the full pension deduction amount, the deduction is reduced by 70% of the exceeding amount. No deduction when pension is higher than:
		  • Local taxes: Single person EUR 16 877; married person EUR 14 473. The amount of pension deduction cannot exceed the amount of pension income.
		  • Government taxes: EUR 3 545.
			IP: pensions (including supplements for adult and child dependants) are subject to taxation, without any special relief for pensions.
			DA: not taxable.
			IB: taxed after six weeks payment in any tax year (including supplement for adult dependants but excluding supplements for child dependants).
				Pensions are subject to taxation. General taxation rules.

Table 5.A1.1. **Main characteristics of disability benefit and taxation systems, as at 1 July 2006** *(cont.)*

	DENMARK	FINLAND	IRELAND	NETHERLANDS
Social security contributions	Disability pension: no social security contributions. Waiting allowance: contributions to the supplementary pension scheme (ATP).	Sickness insurance premium for pensioners is 1.5% of taxable income. No other contributions.	No social security contributions.	WIA/WAO/Wajong: social insurance contributions for the General Surviving Relatives Act (ANW), the General Exceptional Medical Expenses Act (AWBZ), the General Old-Age Pensions Act (AOW) and the Health Insurance Act (ZVW). The contributions deducted for health have to be refunded by the body that administers the payment of the pension. Furthermore from the WAO-benefit contributions for the Unemployment Benefit Act (WW) are deducted and from Wajong a contribution that equals the WW-contribution.
Accumulation of benefits with earnings	Accumulation possible, but with benefit reduction.	• National pension (*Kansaneläke*): pension withdrawn if the take up of work similar to former activity. The pension can be suspended for 6-24 months if the pensioner finds employment. • Statutory earnings-related pension (*Työeläke*): within certain limits, the pensioner is allowed to work while receiving the pension. In the case of full disability pension, if earnings are 40% but not 60% of the pensionable salary, the full disability pension is changed to a Partial disability pension. If earnings exceed 60% of the pensionable salary, the pension is withdrawn.	IP: accumulation with earnings from work is not possible. Invalidity pension requires permanent full incapacity. DA: weekly income disregard of EUR 120. 50% of earnings between EUR 120 and EUR 350 will also be disregarded.	If a beneficiary finds suitable employment, the disablement category, in which she/he has been classed, may change, depending on what he/she earns doing this work. This means that the rate of benefit may be revised.
Tax credits	No special relief for pensions.		No special relief for pensions.	Tax benefits to supplement income or alleviate the burden of the costs for health care (special costs of not insured care (*e.g.* dental care), costs of insurance benefits, diet, transport, facilities, etc.). Tax deductions for a person having excessive health care costs. Specific tax deduction for people on Wajong benefits.
Combination with other benefits	Accumulation is not possible concerning benefits targeted at covering the same maintenance need.	Only one pension from National Pension Scheme may be paid. If combined with a statutory earnings-related pensionor employment injuries & acute or occupational diseases & acute pension, the national pension is reduced. The statutory earnings-related pension is secondary to the employment accident insurance benefit, and only the part of earnings-related pension in excess of the compensation under employment accident insurance is payable. The same applies to compensations under the motor liability insurance. The disability pension (*Työkyvyttömyyseläke*) is not usually granted until the sickness benefit has been paid for the maximum period. This does not apply to the individual early retirement pension.	IP is not payable with any pension under the social welfare acts with the exception of Disablement Benefit (Occupational Injury Benefit). DA is not payable with any pension under the social welfare acts with the exception of Disablement Benefit (Occupational Injury Benefit). One-Parent Family Payment (single parents) claimants may accumulate their One-Parent Family Payment with half the personal rate of IB. IP, DA and IB claimants are eligible for Back-to-Work Allowance and Back-to-Education Allowance schemes.	If disability benefits, together with any unemployment benefits, are lower than the social minimum, a supplement can be claimed under the Supplementary Benefit Act (*Toeslagenwet*, TW) (means tested).

Source: OECD (2007b), MISSOC and information provided by national authorities.

Figure 5.A1.1. **Net replacement rates for disability benefits, unemployment benefits and social assistance, couple households, 2006**[a, b]



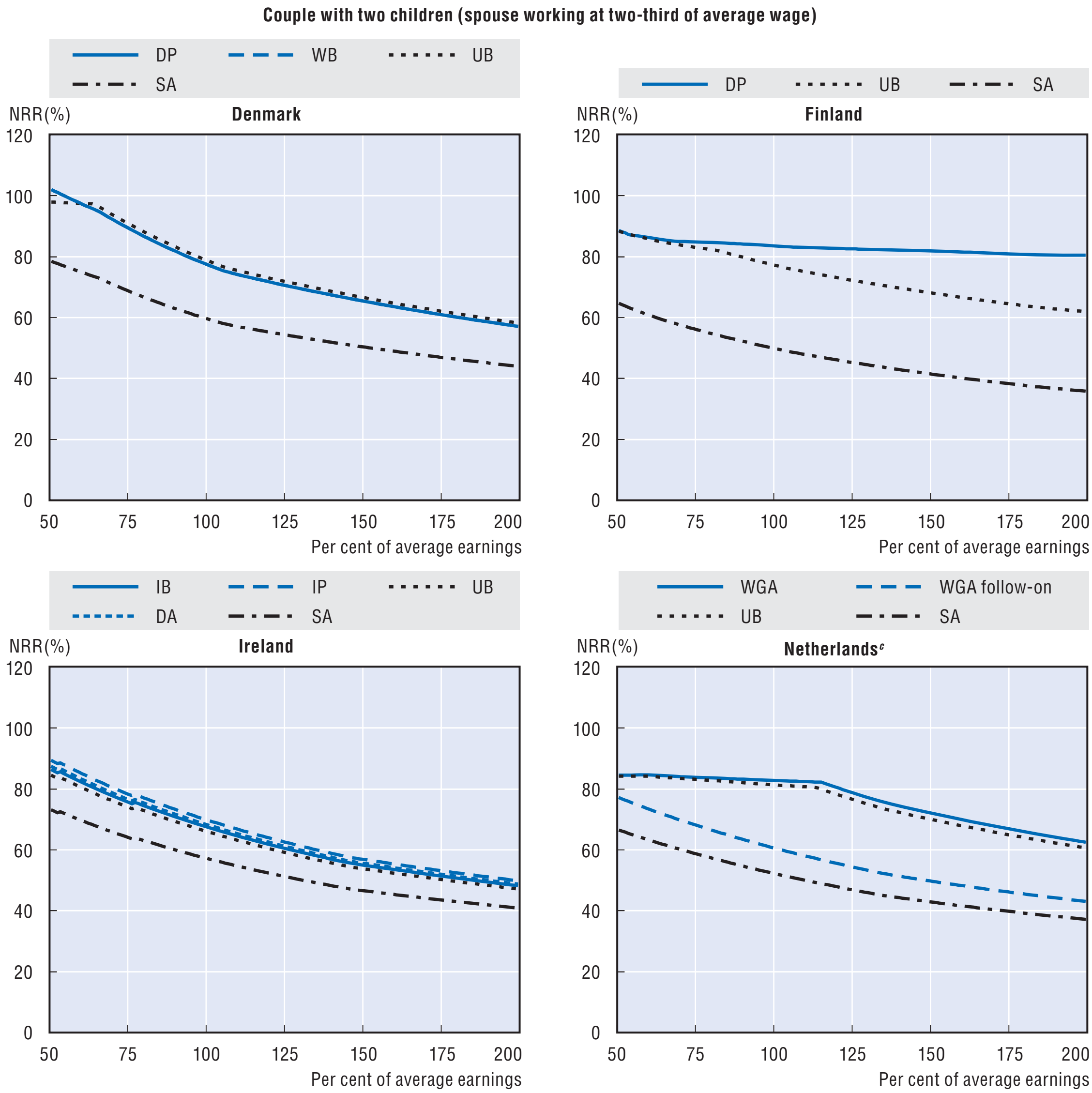
a) Net replacement rates: ratio of household net income after becoming inactive and receiving disability benefit or unemployment benefit or social assistance to household net income when earning 50-200% of average earnings. Estimates refer to a 40-year-old person with an earnings history of 22 years at average earnings. Percentage of average earnings refers to pre-disability earnings of the first earner.

b) DA = disability allowance; DP = disability pension; IB = illness benefit; IP = invalidity pension; SA = social assistance; UB = unemployment benefit; WB = waiting benefit; WGA = initial disability benefit in the Netherlands; WGA follow-on = subsequent disability benefit in the Netherlands.

c) WGA: person assumed to have 79% work incapacity, without receiving top-up social assistance payments.

Source: Special module of OECD tax/benefit model. Information provided by national authorities.

Figure 5.A1.1. **Net replacement rates for disability benefits, unemployment benefits and social assistance, couple households, 2006**[a, b] *(cont.)*



a) Net replacement rates: ratio of household net income after becoming inactive and receiving disability benefit or unemployment benefit or social assistance to household net income when earning 50-200% of average earnings. Estimates refer to a 40-year-old person with an earnings history of 22 years at average earnings. Percentage of average earnings refers to pre-disability earnings of the first earner.

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List of Acronyms

ADHD	Attention-Deficit Hyperactivity Disorder
AETR	Average Effective Tax Rate
ALMP	Active Labour Market Programmes
AMS	Danish National Labour Market Authority
AW (APW)	Average Worker (Average Production Worker Wage)
BTWA	Back-to-Work Allowance
BVG	Shared One-Stop-Shop Premises of Different Actors (Netherlands)
CBS	Statistics Netherlands
CE	Community Employment
CPB	Bureau for Economic Policy Analysis (Netherlands)
CSR	Corporate Social Responsibility
CWI	Work and Income Agency (Netherlands)
DA	Disability allowance
DB	Disability benefits
DETE	Department of Enterprise Trade and Employment (Ireland)
DHC	Department of Health and Children (Ireland)
DSFA	Department of Social and Family Affairs (Ireland)
ECHP	European Community Household Panel
EFILWC	European Foundation for the Improvement of Living and Working Conditions
EPL	Employment Protection Legislation
ESF	European Social Fund
ESRI	Economic and Social Research Institute (Ireland)
ETK	Finnish Centre for Pensions (Finland)
EU	European Union
EULFS	European Union Labour Force Survey
EUR	Euros
EU-SILC	European Union Statistics on Income and Living Conditions
EWCS	European Working Conditions Survey
FÁS	Public Employment Service and Training Authority (Ireland)
GDP	Gross Domestic Product
GP	General Practitioner
IB	Illness benefits
IDS	Income Distribution Statistics (Finland)
IP	Invalidity pensions
IRO	Individual Reintegration Plan (Netherlands)
IVA	Income Provision Scheme for People Fully Occupationally Disabled (Netherlands)
KELA	Social insurance institution (Finland)

LAFOS	Labour Force Service Centres (Finland)
LES	Local Employment Service (Ireland)
LFS	Labour Force Survey
METR	Marginal Effective Tax Rates
MEV	Macro Economic Outlook (Netherlands)
MISSOC	Mutual Information System on Social Protection in the EU Member States
NDS	National Disability Strategy (Ireland)
NRR	Net Replacement Rate
OECD	Organisation for Economic Co-operation and Development
OHS	Occupational Health Services
PES	Public Employment Service
PPP	Purchasing Power Parities
QNHS	Quarterly National Household Survey (Ireland)
REA	Act on the Reintegration of the Occupationally Disabled (Netherlands)
SER	Social and Economic Council (Netherlands)
SFI	National Centre for Social Research (Denmark)
SME	Small and Medium Enterprises
STM	Ministry of Social Affairs and Health (Finland)
STP	Specialist Training Provider (Ireland)
SZW	Ministry of Social Affairs and Employment (Netherlands)
USD	United States Dollar
UWV	Employee Insurance Authority (Netherlands)
Wajong	Work-Disability Provision for Young Disabled Act (Netherlands)
WAO	Disability Insurance Act (Netherlands)
WAZ	Self-employed Person's Disablement Benefits Act (Netherlands)
WGA	Return to Work Scheme for the Partially Disabled (Netherlands)
WIA	Labour Capacity Act (Netherlands)

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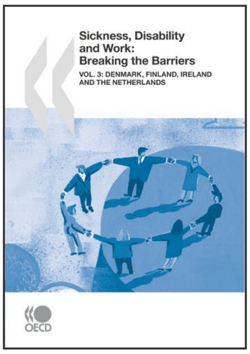

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