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European Unemployment Insurance?

A more modest approach in the short term, more ambition in the long term

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European Unemployment Insurance?
A more modest approach in the short term, more ambition in the long term

Günther Schmid (1)

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Abstract

Although European Unemployment Insurance (EUI) has been at the centre of the debate on 'Social Europe' over the last decade, there is still no consensus on the concept, and no specific steps have been taken towards the introduction of such a system. Debate and policies on EUI have ended in a stalemate; this is surprising given the origin of the idea, which was closely related to the first plan for economic and monetary union in the early 1970s. The first expert group deliberating on the social consequences of a monetary union considered it self-evident that, in the long run, a fully-fledged EUI would have to be established, and – explicitly appealing to 'community solidarity' – that, in the short term, immediate steps would need to be taken in this direction. The question therefore arises as to why this early consensus has faded away, and how this conceptual and political stalemate could be overcome.

This essay starts with a historical overview identifying three waves of the debate on EUI and two current mainstream concepts: a 'genuine' and a 'reinsurance' EUI-system. The pros and cons of these alternatives are discussed. The paper argues that the concept of unemployment insurance itself needs to be fundamentally revised, since modern labour market policy has to cover not only income risks related to unemployment, but also other serious income risks related to critical transitions over the life course, thus opening up the perspective of 'employment insurance' or 'work-life insurance'. Günther Schmid then develops ideas for covering a broader spectrum of social risks, and proposes an enhancement and extension of the existing European Social Fund (ESF), to create a 'European Employment and Social Fund' (EESF), with elements of a genuine European employment insurance as well as a reinsurance mechanism for asymmetric shock absorption.

Introduction (2)

'A community initiative in the unemployment field is particularly opportune, for it will have beneficial effects on the economy and society as a whole. Without waiting for ambitious programmes of generalized harmonization to become operative, one definite step in this direction might be to prove before public opinion that community solidarity is a reality [...]' (Marjolin *et al.* Report 1975)

This appeal to 'community solidarity' appeared more than 40 years ago (3), yet remained largely without a proper response: one of the reasons for the current populist anti-European movement. The Marjolin Report, which aimed to draw up a study of Economic and Monetary Union in 1980, in line with the Werner Plan (4), decisively recommended fully-fledged European Unemployment Insurance (EUI) in the long term, and immediate steps in this direction in the short term. In retrospect, it is even more astonishing that the proposal had 'the agreement of all the members of the group', made up of 15 persons of various European nationalities and professional backgrounds (5). This agreement, however, dissolved in the course of events and most of today's mainstream economists, including those inclined to the 'left' (6), claim that a genuine EUI would not make sense.

The Werner Plan did not foresee the turbulence of the 1970s, following the collapse of the Bretton Woods system and the so-called Oil crises (1973, 1979/80), which put inflation at the top of the agenda. The unemployment issue only re-emerged when the idea of monetary union resurfaced in the European political debate at the end of the 1980s and the beginning of the 1990s (7). But there was no return to the earlier consensus among the scientific community, or at least, not in its previous form. The only partial agreement to emerge from this debate was the idea that a macro-economic stabilisation mechanism would be beneficial for managing asymmetric shocks when, with a common currency, depreciation of national currencies would no longer be an option. The most comprehensive and influential report of that time, the Emerson Report, concluded that the EU's 'structural Funds in general could support the adjustment capacity of regions' and that the 'negative consequences of

2. I am very grateful for the thorough internal review and helpful comments on the first draft of this paper from Francesco Corti, Slavina Spasova and Bart Vanhercke at the European Social Observatory. Many thanks go to the two external reviewers, for their encouragement on the second draft and the hard nuts they left me to crack for this final version. I finally thank Rachel Cowler for improving the English. All remaining weaknesses and mistakes remain my responsibility.
3. Marjolin *et al.* (1975), preface.
4. At the European Summit in The Hague in 1969, the Heads of State and Government of the European Community agreed to prepare a plan for economic and monetary union. The resulting report was drawn up by a working group chaired by Pierre Werner, Luxembourg's Prime Minister and Minister of Finance; https://en.wikipedia.org/wiki/Werner_Plan , download 21/02/2019.
5. The group included, among others, the hard-core neoliberal economist Herbert Giersch from the International Institute of World Economics (Kiel).
6. For example, the German economist Peter Bofinger.
7. For a broader discussion of the history of EUI debate, see Strauss (2016).

shocks could be countered through Community shock-absorption mechanisms'. It did not, however, explicitly refer to a basic EUI as a possible solution ([8]).

The severe recession in 2008/09, then, prompted the third wave of debates on EUI. Even slightly earlier, the Berlin economist Sebastian Dullien (2007) suggested a genuine EUI in the spirit of the Marjolin Report, whereas most of the official European Commission papers stopped at recommending stabilisation mechanisms, without explicitly committing to the idea of EUI. The most prominent voice, the report of the Five Presidents, headed by Jean-Claude Juncker ([9]), was explicitly cautious: ' […] all mature Monetary Unions have put in place a common macroeconomic stabilisation function to better deal with shocks that cannot be managed at the national level alone', but the 'exact design of such euro area stabilisers requires more in-depth work' ([10]). Moreover, and to the disappointment of progressive supporters of a Social Europe, this report also chose not to echo the appeal for solidarity in the Marjolin Report. Progress, we were told, 'must happen on four fronts': towards a genuine Economic Union, Financial Union, Fiscal Union, and Political Union (Juncker *et al.* 2015: 4-5); progress towards a 'Social Union' was not mentioned in this 'to-do list'.

In the meantime, much 'in-depth work' has indeed been done on several fronts, yet the debate is still no closer to a clear vision of how solidarity related to unemployment risks could be institutionalised at European level. The present essay is intended to contribute to such a vision in three steps. First, I outline the state of the debate on EUI in a systematic way, discussing the pros and cons of the main existing alternatives (Section 1). In Section 2 I argue, based on this critical overview, that the concept of unemployment insurance itself needs to be fundamentally revised, since modern labour market policy has to cover not only income risks related to unemployment, but also other serious income risks related to critical transitions over the life course, thus opening up the perspective of 'employment insurance' or 'work-life insurance.' Third, I claim that in order to cover a broader spectrum of social risks, the best strategy in the current political stalemate would be to enhance and extend the existing European Social Fund (ESF), creating a 'European Employment and Social Fund' (EESF), with elements of employment insurance as well as a reinsurance mechanism for asymmetric shock absorption (Section 3). I conclude with a summary (Section 4).

8. Emerson *et al.* (1990), 169; the report, however, mentioned some papers going beyond mere 'shock absorbers' and involving some kind of – at least intermediate – redistribution between rich and poor regions, e.g. van Rompuy *et al.* (1990).
9. Report by Jean-Claude Juncker in close cooperation with Donald Tusk, Jeroen Dijsselbloem, Mario Draghi and Martin Schulz.
10. Juncker *et al.* (2015, 14).

1. State of the debate on European unemployment insurance

> *'[I]n the process of creative destruction, restrictive practices may do much to steady the ship and to alleviate temporary difficulties. [...] Practically any investment entails, as a necessary complement of entrepreneurial action, certain safeguarding activities such as insuring or hedging. [...] There is no more paradox in this than there is in saying that motorcars are traveling faster than they otherwise would because they are provided with brakes.'* (Schumpeter 1976: 87-89)

As Joseph Schumpeter tells us, the concept of insurance as an effective hedging mechanism for innovative investments is not new. In fact, it goes back to the Venetian merchants in the 15th century and is even viewed among economic historians as the crucial driver of capitalism ([11]). This idea has been extended by Karl Polanyi's argument that economies are submerged in 'social relationships,' driven by motives of 'social standing', 'social claims' and 'social assets' (Polanyi 2001: 48); this approach was later recast in the principles of social insurance best summarised by Nicolas Barr (2001: 33-49) and the Nobel Prize winner Peter Diamond (1999: 21-22). These principles, it seems, were known to the 15 experts who contributed to the abovementioned Marjolin Report. An economic and monetary union requires, they said, among other things, 'the existence of centralised fiscal and social security systems ensuring a certain degree of redistribution, including redistribution between the regions' ([12]). Since their proposal sank almost into oblivion, it seems important to present their arguments in some detail, as they are still relevant to the current situation.

A common currency leads to a speeding up of structural change through innovative investments in an open and enlarged market, thereby contributing to asymmetric shocks among the currency members. This understanding was the background to their judgment that the new European 'motorcar' urgently needed additional 'suspension' and 'brakes'. There are two main reasons for a EUI, the experts argued. First, there is the opening of markets and the effects of specialisation and geographical relocation, which lead to 'frictional unemployment which ought to be the responsibility of the Community'. Second, the interdependence of the economies leads to a 'rapid transmission of fluctuations in activity' which should be 'cushioned for the benefit of all by the automatic compensatory movements of such a system.' Furthermore, Marjolin *et al*. envisaged the danger of 'competitive depreciations creating a chaotic situation in the exchange markets [...]. One of the problems which Europe must try to avoid is the creation of excessive tensions between countries with surpluses and those with deficits in their current balance of payments' ([13]).

Although it would not be possible soon to establish a fully-fledged EUI-system, because this 'would require a harmonisation of national systems, [...] a temporary solution must be put into effect in the

11. The clearest proponent of this argument is Bernstein (1996).
12. Marjolin *et al.* (1975: 27).
13. Marjolin *et al.* (1975: 10).

near future [...] which would operate in accordance with the following principles: The Community Fund would be an independent administrative body directed with the participation of the social partners [...]. Each unemployed person [...] would receive as a first part of his payment a Community allowance which would be clearly visible as such. Within an initial period, this allowance could be fixed at a set amount [...] ([14]). On the basis of this first part, the National governments would be free to adjust at their discretion contributions and allowances paid under their national systems. The Fund would be fed by a contribution from income paid in part by employees and in part by employers [...].' In a second stage, the report continues, 'one could conceive a system which would constitute a combination of fixed amount and a percentage of the last wage received in employment [...]. In a third stage, in the more distant future, it would be necessary to establish a standard Community system. Action in the field of employment evidently cannot be limited to the unemployment allowances aspect alone. An indispensable concomitant consists in an active employment and occupational training policy. In effect it is necessary to avoid perpetual structural imbalances and facilitate both possibilities of adaption and occupational retraining and also create employment in backward regions' ([15]).

This straightforward argumentation was not present in the second wave of the debate on EUI. In addition to the aforementioned Emerson Report, further proposals were made as preparations for EMU began in earnest. Majocchi and Rey (1993) developed the idea of a 'conjunctural convergence facility' financed by a 'contingency fund' from ad hoc contributions by Member States. The mechanism would be activated in a discretionary manner, and subject to the condition that the shock must not be due to policy failures of the Member State asking for funds. Furthermore – and relevant to this essay – it was expected that this facility could be activated less frequently if the instruments for addressing the problems of the economically weakest countries were enlarged through the strengthening of structural funds, including the ESF. Italianer and Vanheukelen (1993) added a variant to this: an automatic stabilisation mechanism also addressing asymmetric shocks, and therefore implying an insurance function in the narrower sense. The theoretical basis for this was later refined, and empirically assessed through simulations, by Bajo-Rubio and Díaz-Roldán (2003) ([16]).

The third wave of studies was a reaction to the financial crisis of 2008/09 and, later, to the slow recovery of the European economy. The Euro, introduced in 2002, did not bring the expected convergence, but, rather, divergence. After initial promising signs – Member States' unemployment rates converged until 2007 – the Great Recession crushed such deceptive hopes. Although the

14. The suggestion was two 'units of account' (i.e. in today's currency, two Euros) per day for each unemployed person.
15. Marjolin *et al.* (1975: 34-35).
16. The advantage of this later paper is the lucid distinction it makes between the stabilisation and insurance functions, plus its strong argument for a centralised (EU) fund based on theoretical arguments and empirical studies; the design of the proposal (changes in unemployment are seen as the only important factors for the automatic triggers), however, leads to the paradoxical result that Member States with low unemployment (e.g. Luxembourg) would be subsidized by Member States with (chronically) high unemployment, such as Spain.

European economy seems currently to be in recovery, there are still serious divergences in economic capacities and living standards ([17]). 'Europe today is more imbalanced than before, in terms of the growth potential of its various parts. The core and periphery of the Eurozone have become more divided, and the employment and social situation perfectly exemplify this polarisation' (Andor 2016: 3). Structural change through digitalisation and the ageing of the European population may further aggravate the situation. In addition, as at least some countries (e.g. Germany) face a shortage of skilled labour, there is an impending threat of ruinous competition between Member States for human capital. Already in the last decade, weak Member States in particular – due to high youth unemployment – experienced enforced emigration of young and educated people; this erodes, in the short term, the tax base of their home countries, and also reduces the latter's long-term economic potential through a worrying loss of human capital (Andor 2016: 4). In short: since the beginning of the second decade of this century, the idea of Europe has been in great danger.

This dire situation led the European Commission, as well as the European Parliament, to engage in renewed activity and commission studies on unemployment, and in particular on macroeconomic stabilisers. A recent and comprehensive summary review of these activities identified two concurrent models: a 'genuine' European unemployment benefits scheme, and a 'reinsurance' scheme ([18]). Under the 'genuine' scheme, unemployment benefits are transferred directly to the unemployed individuals, and – in turn – contributions are collected from employers and employees. The 'reinsurance' scheme, however, provides additional funding of national systems in difficult times; this allows for more aggressive counter-cyclical policies, but the benefits are paid out by national benefit systems. This review examined no less than 18 variants of EUI, of which 14 were 'genuine' and four were 'reinsurance'-type systems. In the following paragraphs, I examine only the most prominent proposals.

As mentioned above, the Berlin economist Sebastian Dullien (2007) made, early on, the clearest proposal for a 'genuine' unemployment scheme. Later, his proposal was, largely, taken on by the former Hungarian European Commissioner for Employment, Social Affairs and Inclusion, László Andor. Dullien envisaged a uniform EUI, which would offer all European citizens a relatively modest level of social protection (about 50 percent of wages) for the first six to 12 months of unemployment. National unemployment insurance (NUI) would possibly supplement or extend the benefits. The proposal was intended to fulfil two functions: first, macroeconomic stabilisation; second, and echoing the appeal by the Marjolin Report, transnational improvement of Europe's image among national citizens, who would identify with it, seeing it as an effective and visible actor of their social protection.

17. For the most recent state of the art see Eurofound (2018), which finds some steady convergence related to the activity rate, education-related indicators (early school-leavers and tertiary educational attainment rates), gender gaps in education and in employment, and the job-quality indicators; yet with regard to the employment rate, all labour market exclusion indicators, in-work poverty and material deprivation, the study finds – apart from cyclical fluctuations – growing disparity.
18. See Beblavý and Lenaerts (2017).

The main argument behind the first function is that most studies find that unemployment benefits are among the most effective ways to maintain and create additional demand during economic recessions. As a EUI system would ensure a high coverage rate of unemployed citizens in all Member States, counter-cyclical stabilisation of economic activities would be more effective than, for instance, other conventional stabilisation measures such as tax cuts.

This model, however, is not possible under current European law. It contravenes Article 125 of the Treaty on the Functioning of the European Union (TFEU), which precludes the Union being liable for or taking on the commitments of Member States ('no-bail-out clause'). Moreover, Article 153 (4) TFEU states that the right of Member States to define the fundamental principles of their social security systems shall not be affected. For this reason, László Andor (2013) modified Dullien's original proposal, focusing instead on the stabilisation function, whereby the European Union (EU) could intervene through the so-called flexibility clause, according to Article 352 (1) TFEU. This interpretation, however, is contested. According to this proposal, two thirds of Member States' expenditure for the first six months would be reimbursed from a EUI-fund; any expenditure beyond six months would – in principle – be borne by the Member States. The EUI-fund would be financed from Member State contributions, whereby Andor's proposal would allow only net financial streams. Thus, if countries are exceptionally hard-hit by unemployment, net contributions from the countries less affected would finance unemployment benefits in those Member States whose national funds were not sufficient to offset the economic shock for all (short-term) unemployed. This would reduce the political pressure on those countries to reduce – pro-cyclically – wage replacements in a situation of excessive unemployment in which additional effective demand would be required. Regulation of contributions would ensure a balanced budget in the medium term, to prevent permanent asymmetric transfers.

The supporters of *reinsurance* – prominently, for instance, the think tank Centre for European Policy Studies (CEPS) – start from the idea that social insurance should, at least currently, remain in the hands of the Member States. They take, in particular, European citizens' attitude towards risk-sharing quite seriously, and hint further at the complexity of harmonizing NUI schemes. A genuine EUI, scholars such as Frank Vandenbroucke argue, 'would impose centralized policy decisions on the details of unemployment benefit systems, and contradict widely supported principles of subsidiarity which accommodate diversity in our national social systems. From a technical point of view, the complexity of harmonizing national systems so that they can be (at least partially) replaced by a genuine European scheme should not be underestimated. Re-insurance schemes are in that sense easier and likely more acceptable. Since disbursements of support in a re-insurance scheme are normally based on a trigger […], re-insurance can be set up with the objective to cover only large shocks rather than any cyclical movement. In general, re-insurance allows more flexibility in the design of a scheme' (Vandenbroucke *et al.* 2018: 26). Europe's task, in this view, can only consist in institutionally ensuring the macroeconomic capacity to run such insurance schemes. Since an economic crisis can hit the EU members in varying degrees ('asymmetric shocks'), buffers are required for needy members in order to prevent downward spirals that could – due to economic interdependencies – spill over into the whole of Europe ([19]). Member States should therefore pay 0.1 percent of their GDP into a stabilisation fund until a critical mass of 0.5 percent of euro area GDP is reached. A country ending up in difficulties can receive transfers from this pool, if its short-term unemployment rate is two or more percentage points above the average, defined on a quarterly basis, and in terms of difference from a norm over a reference period of ten years. In order to prevent long-term one-sided transfers, those members who unduly use this pool would pay higher contributions, e.g. 0.2 instead of 0.1 percent ([20]).

Most interesting, finally, is a recent proposal based on an initiative of two members of the European Parliament (Jakob von Weizsäcker from Germany and Jonás Fernández from Spain); the model has been worked out and empirically tested by Sebastian Dullien and Daniel del Prado (2018). The basic concept is a mix of self-insurance and reinsurance, which can be found – as the authors note – for instance in car insurance. In this case, a significant share of the insurance is self-insurance. After an accident, the insurance premium increases, allowing for a substantial share of the losses to be paid back to the insurance company over time; on the other hand, in case of accidents with serious damage, the losses incurred are absorbed to a large extent by the insurance company.

By analogy, in a EUI, Euro area Member States would pay 0.1% of GDP per year into a common European unemployment fund. The lion's share of this would go into a national compartment earmarked specifically for that particular country: the self-insurance compartment. The rest would go into a common 'stormy day' compartment for very large shocks, for the purpose of reinsurance. If a Member State experiences a rise in unemployment above a set of reference values (say 0.2 percentage points), it would receive a net pay-out from its national compartment to help with the increase in unemployment benefits. If a country is hit by a very large economic shock (say a more than two percentage point rise in unemployment), it would receive additional payments from the stormy day fund as re-insurance.

Each participating country would be allowed to run a cumulative deficit in its national compartment of up to two per cent of its GDP. In the first instance, this deficit would be financed by loans from other national compartments. In the event that all national compartments were depleted, the scheme would replenish funds as needed by borrowing on the financial markets. To cover this contingency, the scheme would have a mandate to issue bonds, backed by future contributions as collateral. Dynamic, risk-based adjustment of contributions would be built into the system, to dispel

19. Vandenbroucke argues, in a similar vein, using the powerful metaphor of vaccination: 'with a view to efficiency, it is rational for governments to subsidise vaccinations and/or make them compulsory' (Vandenbroucke 2017: 155).
20. See the corresponding background papers by Beblavý and Lenaerts (2017); Beblavý *et al.* (2017).

concerns regarding the possibility of permanent transfers. The study by Dullien and del Prado also demonstrated, through simulations of past developments, that this scheme has significant stabilisation potential, with minimal net costs to the net contributors under simulation conditions.

These reinsurance models, in particular the last one referred to, represent considerable progress towards the idea of EUI. It is therefore justified to place this concept on the priority list for a future 'roadmap' to implement the European Pillar of Social Rights (Vanhercke *et al.* 2018: 167). Despite their value, however, each of these models starts from two problematic assumptions. They focus mainly, first of all, on the stabilisation function, and less on the two main functions of unemployment insurance: ensuring decent income security, and quick and sustainable reintegration into the labour market to prevent long-term unemployment ([21]). Second, they envisage unemployment insurance only in its narrow sense. National as well as European considerations of social security, however, must consider that labour market risks no longer consist only of unemployment. Increasingly, there are further wage income risks related to critical transitions over the life course ([22]). Examples of these are income volatility due to variations in working time buffering seasonal and business cycles; the erosion of adequate vocational or occupational skills during a working lifetime; reduced or diminishing work performance due to illnesses or ageing or caring in mid-life. Last but not least, it should be possible for a worker to build up financial resources in the form of individual accounts or drawing rights, in order to enhance his or her ability to freely choose work places and occupations not only at the beginning but also during his/her life course. It is high time that the European labour market becomes mature and that individual workers have a stronger voice in shaping their employment relationship ([23]).

Thus, the debate about EUI puts us in a tricky situation. Whilst the 'United States of Europe' is only wishful dreaming, the main responsibility of income security must – according to the current state of EU law – remain with national unemployment insurance schemes. Yet the weaknesses of these systems cannot be overlooked. Many EU Member States have only rudimentary systems of wage replacement in the case of involuntary unemployment. Although the average coverage rate (here the percentage of insured individuals in the labour force) in the EU is 73 percent, there is substantial variation across countries (from about 40% in Romania to 100%, for example, in Finland); net replacement rates vary between about 20 and 90 percent and the duration of insurance benefits is between 20 and 120 weeks ([24]) Some of these differences are due to variations in the eligibility conditions, e.g. long employment records, but another substantial factor is the increase in non-

21. This does not mean that the promoters of macro-economic stabilisers neglect this dimension; Andor (2016: 3-4), for example, is quite determined in this respect.
22. This is, in these days, even acknowledged by hard-core neoclassical labour economists, e.g. Cahuc (2018).
23. See in particular Supiot (2016). The European Pillar of Social Rights is also intended to enhance individual sovereignty, e.g. through the right to life-long-learning (European Commission 2017).
24. All figures are related to the year 2010 and based on Esser *et al.* (2013).

standard employment [25]. Moreover, there are now new social (security) risks linked to the digital world of work (work without employers), combined with growing demands for the social inclusion of people formerly only marginally attached to the labour market (mothers, the elderly, the disabled); and a shortage in corresponding institutional capacities to resolve the related social protection problems.

In this complex situation, it therefore seems wise to scale down the ambitions for Europeanisation of domestic social security. In the short term, we should consider what pragmatic steps can be taken, while envisaging, in the long run, more ambitious objectives that go beyond the conventional system of unemployment insurance. Unemployment insurance which also includes other income risks (other than unemployment) in changing situations over the life course could be expressed with a new and future-oriented wording, using the concept of employment insurance in the analytical framework of transitional labour markets (Schmid and Gazier 2002; Gazier 2003; Schmid 2017).

2. Towards a system of European employment insurance

> *'In a system of single market, high income-countries have to support low-income countries or regions (…). In a system of monetary union, surplus countries have to support deficit countries; otherwise, the different problems of moral hazard, on both sides, will inevitably undermine the union'.* (Andor 2016: 12)

First, we have to ask *whether a European element of wage income security should be based on the principle of social or means-tested insurance*. Several arguments speak for the maintenance and enhancement of the social insurance principle discussed at length elsewhere [26]. *Ex ante* risk-sharing is the essence of social insurance, which has at least seven significant advantages compared to *ex-post*, means-tested social security:

1. Social insurance benefits are better protected than means-tested benefits against discretionary political decisions, due to targeted individual or employers' contributions, often complemented by fiscal budgets which are targeted for reasons of redistribution. The method of financing (taxes or contributions) is thereby not the decisive point; the important point is long-term fiscal targeting. The digital revolution, however, may require an increasing share of general tax financing (preferably consumer taxes) to enhance redistributive capacities and relieve wage income, placing a greater burden, instead, on capital income.

25. See, for details, Schmid and Wagner (2017), Schmid (2018), Spasova *et al.* (2017).
26. For an extensive explanation and justification of the concept of employment insurance see Schmid (2015, 2017); and Schmid (2018; 129-148).

2. Social insurance benefits are usually implemented by independent institutional bodies (often in tripartite arrangements), which, over time, develop professionalism that is proof against short-sighted policy intervention.
3. Individual and wage-related benefits can be calculated much more easily and fairly than means-tested benefits.
4. The work incentives of work-related social insurance benefits are stronger than for means-tested benefits, not least due to the entitlement effect.
5. The macro-economic stabilisation impact of wage-related replacements is higher than that of (usually lower) means-tested benefits.
6. Generous short-term unemployment benefits (up to about nine months of unemployment) have various positive external effects: they reduce cut-throat competition between insiders (covered by insurance) and outsiders (not [yet] covered by insurance). They also provide individual workers with the choice to reject non-standard work especially in its precarious forms; and they protect – at least for a reasonable time – people from resorting to costly consumer credit.
7. Jobless people covered by un/employment insurance remain healthier and more self-confident than jobless people without such benefits or with only means-tested benefits.

Two specific strategies follow from the concept of social insurance and *ex ante* risk-sharing. First, not only should work pay, but transitions should also be made to pay by extending social insurance principles beyond the risk of unemployment, to include, especially, volatile income risks associated with critical events over the life course (school-to-work-transitions, job-to-job transitions, working time transitions, and transition from work to retirement) reflected to some extent in non-standard forms of employment. Second, not only should workers fit the market but the market should be made to fit the workers; the capacity of employers and employees to adjust to uncertainties should be enhanced by investing in human capital and in the workplace environment.

The next question is this: *should a EUI be – at its core – a genuine and uniform system, maybe with extra generosity and coverage depending on national traditions, or should the core be the national security systems, with EU-enhanced national institutional capacities*? In the following paragraphs, I argue for the second solution, without excluding the first model. Current national unemployment insurance regimes are so different that agreement on a core uniform system is unlikely in the near future. Moreover, a uniform EUI also entails the danger of further downgrading minimum standards of income security, without guaranteeing complementary efforts and capacities to promote work and employment. In case of a genuine EUI scheme, Member States with well-established systems of unemployment insurance could become inclined to reduce standards and expenditure, whereas countries with less developed systems might restrict themselves to the level of income security ensured and financed by the European system.

That is why at the current stage, the EU should firstly ensure that all Member States create comparable capacities for employment and income security. In the short run, Europe could therefore take on some positive elements of the United States (US) system, in order to enhance the independent national insurance systems and to add to these a European fiscal capacity containing an element of reinsurance and of social insurance ([27]) The reinsurance element would help those Member States whose insurance funds become depleted; the social insurance element would encourage national insurance schemes to include income risks in addition to unemployment, i.e. moving towards employment insurance. In order to accomplish these two functions, a *European Employment and Social Fund* (EESF) could be established, based on the current European Social Fund (ESF) and Globalisation Fund (EGF), but filling them with new life and additional financial resources.

What is the rationale for such a fund? First of all, many Member States have only weakly developed unemployment insurance regimes. They have poor capacities for employment promotion but also scarce resources for wage replacement, the latter aspect being largely underestimated if not neglected by neoliberal economists. It is one of the greatest mistakes of politics and economics to consider unemployment benefits only as a 'passive' transfer, as opposed to so-called 'active' promotion of jobs and requested skills. To both workers and employers, reliable and generous unemployment benefits are anything but passive. They offer not only a fair offsetting of individual risk, whereby a worker can be in difficulties through no fault of his (or her) own, but also an 'active' investment in productive job search. Recent studies – even by the OECD – show that unemployed workers endowed with generous wage replacements in the first six to nine months find more productive jobs than unemployed workers receiving no or only marginal benefits. Even more importantly, these jobs are more sustainable. In other words: generous short and medium-term benefits avoid or mitigate revolving door effects: 'quickly out of and quickly back to benefits' ([28]).

Effective employment services are essential elements of inclusive unemployment insurance schemes. Only such instruments can ensure the necessary matching into new jobs, individual case management and labour promotion. A scheme of effective employment services is also vital for overseeing the moral hazard inherent in any system of insurance, as indicated in the introductory quote to this section ([29]). New evaluation studies unanimously emphasise the importance of implementation capacities for the effectiveness and efficiency of 'active' labour market policies ([30]). Such capacities are lacking in most of the Southern and Eastern European Member States. The

27. For details of the US-UI system see Fischer (2017), Schmid (2018: 169-175), and in particular Wandner (2018).
28. For productivity gains of 'passive' unemployment insurance see, for example, Acemoglu and Shimer (2000).
29. For a broader discussion of moral hazard, including the 'institutional moral hazard' relevant in multilevel-UI systems, see Vandenbroucke *et al.* (2016).
30. For an overview of studies related to 'active' labour market policies and a rigorous empirical study, see Escudero (2018).

populist criticism that money, for example, out of the pockets of allegedly hard-working Germans flows into the pockets of allegedly lazy Greeks is understandable when there is no employment administration able to control moral hazard. Effective employment services, in combination with inclusive unemployment insurance, can also support those enterprises which have to react to large-scale structural changes with staffing measures, in order to maintain or improve their competitiveness. Such services, moreover, can also help to prevent long-term unemployment through targeted labour promotion measures. National unemployment insurance systems which prudently balance support and control increase the capacity of inbuilt stabilisers as well as the capacity of interregional redistribution aimed at comparable European standards of living, thereby also reducing the pressure of migration.

To conclude these considerations, we should remember that support for institutional capacities is already an element of the current ESF, albeit on a tiny scale. This function could be developed further in two directions. First, national unemployment insurance schemes could be helped to include employment risks over and above unemployment, in a move towards employment insurance. Reasons for including such risks are increasing individualisation, demands for greater inclusion on the labour market (e.g. of the disabled or the elderly) and greater working time flexibility over a person’s lifetime (e.g. families with children or frail elderly); another reason concerns the increasing interdependencies between EU Member States and EU policies, in relation, for example to joint ventures for green jobs or combating climate change, which might induce structural disruptions.

Such an enhancement of institutional capacities would already improve the inbuilt stabilisation function of national insurance systems. In emergency situations, however, this would not suffice; the uncertainties of globalisation demand more. The second element, therefore, to be added to the envisaged EESF is a fiscal capacity to enhance the stabilisation function of national unemployment insurance, in deep economic recessions usually involving asymmetric shocks for national members. The provision of low-interest loans to national insurance schemes in deficit would maintain their ability to bridge such critical situations. Alternatively, and in analogy to the US model, an emergency fund could help out, particularly in a symmetric shock situation. Such mechanisms could thus ensure wage income security and thereby uphold effective demand, instead of responding with pro-cyclical reactions such as benefit reduction or even raising contributions or taxes. Such a fund for securing labour market transitions and economic stabilisation would top up rather than replace national unemployment insurance funds.

3. Features of the European Employment and Social Fund

> *'The essential feature of a bridge is that it is a fixed device that lets you transit discontinuity without getting nervous'.* (Cohen and Stewart 1994: 405)

What should and what could the European Employment and Social Fund (EESF) contribute to the requirements for inclusive income security in case of unemployment? For such a fund to be used, minimum standards for national insurance systems would first need to be set. Apart from economic reasons ([31]), there are three (contested) legal bases for adopting the European directives needed for such standards. First, according to Article 153 TFEU, 'the Union shall support and complement the activities of the Member States' in the field of, inter alia, 'social security and social protection of workers'. Second, the aforementioned Article 352 TFEU allows the Council ('acting unanimously on a proposal of the Commission and after obtaining the consent of the European Parliament') to adopt appropriate measures to attain objectives set out in the Treaties, such as full employment, a high level of protection, social progress, justice, cohesion, and solidarity (Article 3 (3) TEU). Although, in the narrow sense, it is not yet a 'legal' source, the '*European Pillar of Social Rights'* – solemnly proclaimed by the European Parliament, the Council of the EU and the European Commission on November 17, 2017 in Gothenburg – can be used as an argument for legitimacy. The Pillar not only proclaims *new social rights,* such as a minimum income guaranteeing a decent life, the right to adequate social protection irrespective of the kind of employment relationship, and the right to life-long learning; it also clearly states that for them 'to be legally enforceable, the principles and rights first require dedicated measures or legislation to be adopted at the appropriate level' (Article 14).

In relation to unemployment insurance, these standards should in particular ensure an appropriate coverage and level of income security. The benchmark for coverage could be two thirds of employees, and the minimum level of insurance for involuntary unemployment could be set at 50 percent of previous gross wages for the first 26 weeks. Also, the minimum duration of wage replacements should be set at least at 26 weeks, possibly – however – six to nine months. Finally, similarly to the German short-time work allowance, there should be a right to social protection in case of working time adjustment due to variations in the business cycle. Such standards would promote a low level of institutional convergence, yet not aim to bring about a (legally precluded) harmonisation of national insurance systems. After discussion, such standards should be decided on a majority basis, leaving Member States the possibility to opt out.

Next, the EESF could support national systems (those which opted in) with repayable loans if they run into deficit, thus enhancing the stabilisation function of national insurance systems. Regulations, and possibly automatic rules (triggers), would have to be negotiated in order to ensure this

31. See again the helpful vaccination metaphor used by Frank Vandenbroucke (2017) which underlines the economic and social rationale for a minimum set of common social security standards in a monetary union.

stabilisation function, e.g. to define 'severe economic recession', maximal indebtedness or the conditions of repayment. In emergency cases, in particular in the event of symmetric shocks (as in 2008/09), additional and direct funding could come from an emergency fund, to ensure quick reaction and the prevention of vicious cycles of income loss and demand deficiency; Member States might be reluctant in such bad times to take out loans, even if they are subsidised, as recently proposed by the Commission's *European Investment Stabilisation Function* (EISF) ([32]). The US example shows that in deep recessions, emergency unemployment benefits plus supplementary unemployment benefits (possibly targeted towards low income workers) funded directly from the federal government made the real difference in the stabilisation of effective demand ([33]).

Furthermore, after 52 weeks of individual unemployment, the EESF could be used to co-finance a transition allowance (TA) in regions with particularly pressing employment problems. This allowance should be used for various purposes related to critical transitions over the life course, and should be directed towards 'active securities'. As phrased in the epigraph at the beginning of this section, which expresses the rationale of transition allowance, people are more willing to tolerate added and demanded flexibility, i.e. to take on risks, if they can rely on bridges to overcome critical discontinuities during their life course; reliance on such institutional bridges can be described as 'moral ensurance'. Most economists, however, are preoccupied by the moral hazard connected with any insurance, which is unavoidable and has to be kept in check. They often neglect the moral ensurance aspect which is also implied by any insurance scheme and has to be enhanced. This holds true for pure insurance schemes without redistribution and even more for social insurance schemes containing additional redistributive aspects ([34]). Examples of such 'moral ensurance' are opportunities to pursue continuous or further training, to combine part-time work and education, wage insurance for necessary transitions into lower paid jobs or to bridge temporary lower productivity for a job paid at the same or higher level, reasonable adjustment of the workplace for disabled people, and – last but not least – the anticipation of reliable public assistance in the critical phase of transiting from waged-work into self-employment.

In principle, such transition allowances should always be co-financed, on average 50/50, by the EU and Member States, allowing for different percentages depending on the economic power of Member States. Financial resources for transition allowances could – as for the current management of the large European structural and social funds – be allocated in the medium-term. In particularly severe recessions, again taking the US system as a model, payment of emergency benefits beyond the

32. Details plus critical comments by stakeholders on this most recent European Commission proposal can be found in Scheinert (2019).
33. With this reference to the US model I am taking up the comments of one of the external reviewers; for evidence see, among others, Schmid (2018, Table 23: 172).
34. Centralised unemployment insurance schemes usually redistribute from high-skilled (at low risk of unemployment) to low-skilled workers (at high risk of unemployment), and, even more so, from rich regions to poor regions. For the theoretical concept of 'moral ensurance' see Schmid (2018: 202-203); Schmid (2019: 160-161).

regular duration of unemployment benefits should not be ruled out. Apart from their social function, the rationale for such benefits is again their investment function. They would also, given the necessary political will at European level, enhance macroeconomic stabilisation in such extreme situations and prevent cut-throat competition between those with benefits and those without. Such emergency benefits could be financed from the reserves held by the EESF or the European Monetary Fund.

In the long-term, an independent EU-levy for financing the EESF would be desirable. The kind of resources to use for such a levy (wages, value added, capital returns) is a matter for discussion. There are important arguments – in particular the further shrinking of the wage base – in favour of financing the EESF from a share of GDP, particularly since EESF expenditure will concentrate on enhancing the infrastructural capacities of national insurance systems, and will only take on inclusion and stabilisation functions in emergencies. These levies should be constructed in such a way that they build up reserves in good times, to be used in bad times. A conservative estimate of the size of the levy would be 0.2 percent of GDP; this would create a fiscal capacity of about 32 billion Euros per year. By way of comparison, the total EU budget in 2018 was about 160 billion Euros, about one percent of GDP; the total ESF budget in 2018 was 13.5 billion Euros. An even more drastic benchmark is to remind the reader that the US Federal Budget 'eats up' about 20 percent of GDP.

The national contributions to the EESF could also include an element of solidarity, directly related to the situation of having a common currency (the Euro) shared by members with differing levels of economic power. If – as is often said – chronic trade surpluses 'export' de facto unemployment, then it would only be logical to link national EESF contributions to these: members with extreme surpluses would pay more than members with a balanced budget or large trade deficits. Such a mechanism – quite apart from its solidarity stabilisation effect – would create an economic incentive to take action against chronic trade surpluses, e.g. substantial wage increases across the whole workforce, higher public investment, or a tax on the capital exports that are usually related to trade surpluses ([35]).

35. This argument, however, has to be handled with some caution. First, it has to be acknowledged that trade deficits do not immediately translate into lower or higher employment. US experiences show, if any, a low correlation between net employment loss and trade deficit; the manufacturing jobs lost as a result of the 2015 US trade deficit represent only 10 percent of all job losses that occurred because of productivity gains (Rose 2018: 10). Second, and as one of the external reviewers remarked, a higher contribution could further depress effective demand in the surplus country and be counter-productive. Yet there is a consensus that the imbalance between the surplus countries and the deficit countries should be addressed. It would, therefore, be useful to have mechanisms that force chronic surplus countries to shift to a more expansionary policy. My argument, thus, is in fact based on the questionable idea that the threat of levying higher contributions might force the surplus country to change policies; further research is required. There seems to be general agreement, however, that directing public subsidies towards supporting structural change (e.g. generous unemployment benefits, pro-active training policies and mobility incentives) is more effective than directing them towards job creation in non-competitive industries (see again Rose 2018: 12).

To be sure, such an independent fiscal capacity requires a change to the EU treaties. It would, however, be necessary, to ensure that both functions for the envisaged system of European employment insurance are adequately fulfilled: reinsurance as well as social insurance. Such a system would also be worthwhile as it would – in connection with corresponding budget sovereignty for the European Parliament – encourage national citizens to identify more closely with Europe. Furthermore, it would intensify the exchange of experiences and good practices between national labour administrations, and the current system of European placement services (EURES) could be extended to create a genuine European Employment Agency.

A first possible step, without having to change the EU treaties, could be to merge the ESF and EGF, already for the mid-term EU budget 2021-2027. The EGF, established in 2007, had a very limited budget for the period 2014-2020 (around 150 million Euros), to support the reintegration of workers who had been victims of mass redundancies from companies with more than 500 employees. Member States applying to this fund had to co-finance 40 percent of the expenditure and the application and administration procedures were quite burdensome. For this reason, even the scant resources of the EGF were not fully taken up. Yet evaluation studies revealed that the projects which took place were quite effective. They resulted in quicker reintegration (volume effect), enlarged the range of measures (scope effect), stimulated mutual learning (role effect), and improved institutional interaction (process effect) ([36]).

Thus, it makes sense to substantially increase the EESF fund during the next programming period, by, for instance, further reducing the Common Agricultural Fund (CAP), and to place strong emphasis on reforming the management of this fund. The current Commission activities related to the so-called ESF+ seem to already be moving in this direction ([37]).

Even if such transfers of investment were to remain quite small, the symbolic value of a genuine transnational employment and income security institution should not be underestimated. Europe would become more tangible for its citizens. Studies show that employees of transnational institutions quickly develop supranational identities, which reduce regional or national idiosyncrasies and ego-centred interests. The EESF in its embryonic phase should prioritise capacity building and employment promotion. The speedy development of a European matching service (EURES) should be the first step, followed by targeted mobility promotion (financial and linguistic support, help in finding housing) for unemployed workers willing to move to other regions or even to another country for a new job ([38]). Targeted employment promotion for young people would be the second priority,

36. See the methodologically fine study by Weber *et al.* (2015).
37. The proposed ESF+ Regulation in the Multiannual Financial Framework (MFF) for the period 2021-2027 is designed to bring together the existing European Social Fund (ESF), the Youth Employment Initiative (YEI), the Fund for European Aid to the most Deprived (FEAD), the Employment and Social Innovation Programme (EaSI) and the EU Health Programme.
38. In the long run, as one of the external reviewers suggested, it could even make sense to develop EURES further into a real European Public Employment Service (EPES).

for example employment support in small and medium sized enterprises (SME) through a combination of cheap investment loans (from the EU's investment and structural funds) and recruitment subsidies. In the current critical situation, a bold wage cost subsidy programme could be open to enterprises who hire workers from the pool of unemployed in regions with special employment problems. It was Nicolas Kaldor, an academic colleague of Lord Keynes, who already hinted at this option. If, he said, employment cannot be boosted by devaluing currencies, wage cost subsidies for each additional or reasonably maintained job would be a functional equivalent. Finally, short-time work to maintain skilled labour should not be ruled out, in particular when combined with upskilling and reskilling.

Such transfers would not only ensure cyclical stabilisation, by maintaining effective demand in the regions badly affected by the crisis, but would also promote social inclusion, by preventing long-term unemployment and relieving the pressure on skilled workers to emigrate. Certainly, more regional mobility is necessary for a well-functioning European labour market, and such mobility is also welcome among parts of the European population, especially young people. This potential flexibility, however, is limited, for various reasons, and is not desirable at all costs, in particular not for adult and elderly skilled workers. In the long term, a European system of employment insurance should not content itself – apart from wage flexibility – with the balancing mechanism of labour mobility often enforced by frictional unemployment, as the neoliberal logic implies. The logic of employment insurance also implies keeping the labour force – if not in the same companies – at least in the local or regional area, through supported further training and working time flexibility, or bringing work to the workers instead of bringing the workers to the work. Such a strategy would also encourage a multi-national and inclusive striving to feel at home in Europe, instead of the currently prevailing nationalist and exclusive need for 'Heimat'.

4. Summary and conclusions

> *'[...] if an ESU is to become a counterpart of the EMU within the overall EU framework, the two unions must gradually come to terms with each other, in a 'logic of institutional complementarity'.* (Ferrera 2018: 19)

What can pull Europe back from the brink? This essay deliberately started with the appeal for solidarity made by the group working with Robert Marjolin (1975), who was among the first to think about the consequences of a common market and common currency. This appeal is echoed, to an increasing extent, in recent studies on the future of 'Social Europe'. Currently, however, as we have noted, a European Social Union (ESU) ([39]) is not on the official EU agenda. However, the need to take the issue of pan-European solidarity, between countries and all European citizens, more seriously is clearly reflected in the growing literature on EUI. The historical review of proposals for transnational unemployment insurance schemes above, however, has confirmed the argument put by Maurizio Ferrera, that establishing pan-European solidarity in the EU will be very different to (and probably even more difficult than) the transnational welfare state development in existing Federal States such as the United States, Canada or Australia. The reason is quite simple. The construction of an ESU has to take place in the context of 'extensive nation-based welfare states', which are endowed with considerable variations and their own institutional backgrounds. For this reason, proposals for a genuine EUI are currently 'off the table', although, and as argued here, not 'out of sight'. They may be a solution in the far distant future, when a unified European labour market exists and when the corresponding legal requirements as well as the political will for a further deepening of Europe are in sight; these conditions, however, are not currently met.

The remainder of this essay demonstrated how the 'institutional complementarities' of EMU and ESU, called for here, could be implemented. More specifically, this paper argued for a relaunch of the established European Social Fund, to move towards a 'European Employment and Social Fund', combining elements of social insurance with elements of reinsurance. These would gradually develop and ultimately be financed by a specific budget, and – possibly – implemented by a separate pan-European agency.

This paper also argued that even the more modest proposals for re-insurance of national UI schemes should be approached with caution. This is because, first, there is still no consensus on them, but mainly because they overemphasize the macro-economic stabilisation function and neglect the genuine objectives of (un)-employment insurance: a) to provide reliable and generous social security in the medium-term; b) supported by an effective employment service including job creation to

39. The notion 'European Social Union' was originally coined by Frank Vandenbroucke (2013), its substance was further detailed in the context of the High-Level Group set up by Friends of Europe (Vandenbroucke with Vanhercke 2014). It was given further flesh to the bones, more recently, by Maurizio Ferrera (2018).

prevent long-term unemployment, and c) – in the spirit of the theory on transitional labour markets – to also cover the growing social risks related to critical transitions over the life course. In the future, insurance schemes covering this third aspect could be labelled as 'employment insurance' or possibly as 'work-life insurance'.

Reasoning based on normative theories of justice and democracy, as well as empirical results from recent surveys, shows that an approach which is more moderate in the short-term but far more ambitious in the longer term (see the subtitle of this essay) could realistically find support among European citizens. Maurizio Ferrera (2018: 26-28) argues that the Euro-scepticism common among the political and intellectual elite might be misguided: there is potentially a 'silent majority' in support of a larger EU budget aimed at promoting economic and social investment, helping people in severe poverty and providing financial help to Member States experiencing rising unemployment.

It is also important to address the issues in the right way. Frank Vandenbroucke *et al.* (2018), using an intelligent recent survey with sophisticated methodology covering various types of approach, found that EU citizens are ready to share the risk of unemployment crises. Fundamental opposition to European unemployment risk-sharing (EURS) is confined to a relatively small segment of the population. European citizens prefer packages that are more generous, and that require countries to offer education and training to all their unemployed citizens. In most countries, support is stronger if the implementation of EURS is decentralized: this confirms the argument of this paper that one should not try to build a genuine European benefit scheme, but rather a reinsurance scheme that supports national benefit systems with lump sum transfers. In all countries, support (even for redistribution) increases if EURS is combined with conditionality, in other words with *social investment* policies such as training, education and activation measures that ensure – apart from enhancing individual opportunities ('moral ensurance') – effective control of 'moral hazard'. And, last but not least, European citizens, when expressing preferences, seem to pay less attention than policymakers to the issue of how tolerant the scheme should be with regard to cross-country redistribution.

In other words, and to sum up: practical and effective policies to mitigate and tackle social risk over the life-course are decisive as an argument for progress towards a European Social Union.

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