Labor Market Reform in Israel and the Flexicurity Option

Dan Ben-David and Liora Bowers*

Abstract

Flexicurity is the name commonly ascribed to a set of labor market and welfare policies, adopted primarily by Nordic countries, providing relatively high levels of hiring and firing flexibility to employers alongside a financial safety net and employability for workers. Flexicurity countries have higher levels and faster growth in labor productivity and the gap between these countries and Israel has been increasing for decades. These countries are also characterized by higher rates of employment and lower rates of poverty and income inequality than Israel – which raises a number of questions, chief among them: is the better socioeconomic performance in flexicurity countries due to flexicurity policies and could this approach be a viable option for Israel? This chapter explores these questions through an examination of the various attributes of flexicurity policies and a comparison of socioeconomic outcomes in flexicurity countries, other country groupings and Israel, and concludes with some relevant policy recommendations.

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The idea for this study emanated from a presentation of the Taub Center's *State of the Nation Report 2013* before the senior staff at the Prime Minister's Office and a subsequent request by that Office for an examination of Flexicurity's possible applicability for Israel. Previous versions of this project were presented in sessions with various members of the Prime Minister's

Introduction

Combining some of the developed world's lowest productivity levels with its highest rates of poverty and income inequality, Israel is situated on socioeconomic trajectories that are unsustainable in the long run. On the other hand, Israel continues to have some of the world's best universities and a highly innovative high tech sector. Foreign direct investments and venture capital continue to stream in at rates that provide only a hint of the country's tremendous potential – if, and when, it will be able to channel the knowledge that it already possesses towards a much larger share of its population. Israel's rapidly changing demographic landscape still provides a window of opportunity, albeit a steadily narrowing one, for harnessing the country's unique resources before it crosses a point beyond which it will be unable to adopt policies that are already challenging to implement today.

The country is in urgent need of a systemic reset of its national priorities, from its current acquiescence to sectoral, business and personal pressures and interests towards a comprehensive plan targeted at its core challenges and their underlying determinants. Ben-David (2014) provides an outline of what such a plan should entail. It is based on three policy spheres that together require general budgetary reprioritization. The first policy sphere focuses on the need to restructure incentives – from non-work to pro-work incentives, and for employers to hire from the existing pool of Israelis as opposed to importing unskilled and uneducated workers from abroad – while providing a comprehensive employment package yielding the skills necessary for contending in an open economy.

Office, cabinet ministries and the Bank of Israel. We would like to thank Adi Brender, Roie Dror, Haggay Etkes, Michal Fink, Eugene Kandel, Ayal Kimhi, Lilach Lurie, Guy Mundlak, Ehud Praver and Michal Tzuk for their useful comments and suggestions and Hadas Fuchs and Kyrill Shraberman for data assistance. The final determination of what to include in this chapter and the recommendations in it were made by the authors alone.

The second policy sphere addresses the need to create a supportive surrounding environment for those whose incentive structures have changed, and who have picked up elementary skills that can enable them to put their foot in the economic door and gradually open it further. The third policy sphere emphasizes the strategic perspective, including, but not limited to: budget transparency to enable a rechanneling of scarce resources; fundamental educational reform ranging from implementation of a considerably upgraded core curriculum that effectively prepares individuals for entry into a fiercely competitive global labor market and a modern democratic society to improved methods for selection, training and compensation of teachers; and heightened law enforcement aimed at reducing a shadow economy currently estimated at over one-fifth of Israel's GDP (Gruber, 2014).

This chapter delves deeper into elements highlighted in Ben-David's (2014) first policy sphere in the comprehensive plan, analyzing possible policy routes in this vein. Specifically, the objective here is examine the applicability for Israel of a concept commonly known as flexicurity, a strategy intended to increase labor market flexibility for employers while providing financial security and employability for labor force participants (not to be confused with job protection in a specific place of work). This is a system currently in place – in one form or another – in Nordic countries and in the Netherlands (together, the "Flexicurity countries" or "Flexicurity model"). Along with providing history and background on flexicurity, this chapter classifies Israel and other Western countries according to various flexicurity indicators and discusses relevant social and policy implications for Israel if it were to adopt aspects of the traditional flexicurity system.

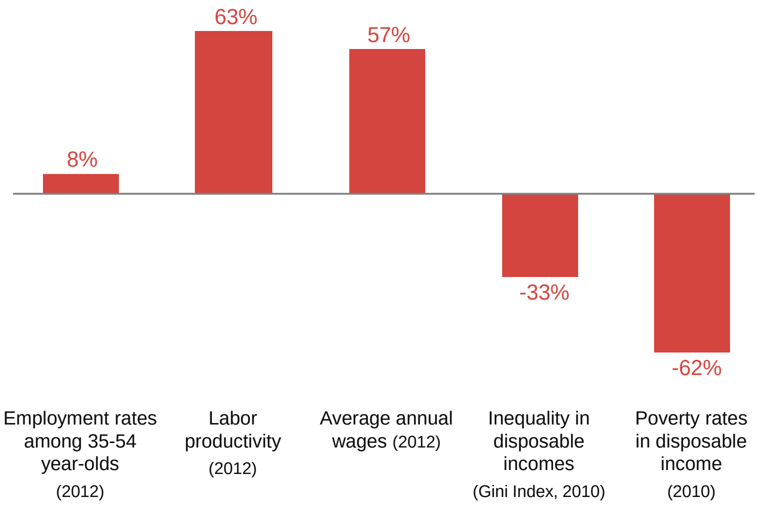
1. The Danish Example

One of the Nordic countries, Denmark, has in fact become somewhat of a poster country for the flexicurity system. A socioeconomic comparison of Denmark to Israel using a number of different measures (Figure 1) provides a glimpse of the differences between the two countries. Employment rates among prime working-age men aged 35-54 in Denmark are 8 percent higher than in Israel. A larger labor force means greater output for the same population, which in turn translates into higher GDP per capita (i.e., higher living standards for the Danish population).

Figure 1

A socioeconomic comparison of Denmark and Israel

percent differences between Denmark and Israel*



* Calculated as the percent difference in the measures for Denmark minus the measures for Israel

Source: Dan Ben-David and Liora Bowers, Taub Center

Data: OECD

Not only are Danish employment rates higher, so is labor productivity, which is defined as GDP produced per hour worked. The average Danish worker produced 63 percent more than the average Israeli worker during each hour worked in 2012. This finding has two major implications. First of all, while addressing business cycles (recessionary periods versus inflationary periods) around the long run trend is important, the primary determinant of the entire trend – i.e., the main factor determining the height and the slope of a country's long run multi-decade economic growth trajectory – is productivity. A key measure of productivity is labor productivity, which is the focus here and which has a direct link to wages. If a worker does not produce much per hour (that is, low worker labor productivity), then it is not possible for that worker to receive high wages since there is no source from which to draw upon to provide high wages. Though high productivity is insufficient for guaranteeing high wages, rising productivity is certainly a necessary condition for incomes to rise. Hence, it should come as no surprise that Danish wages are 57 percent higher than Israeli wages.

While faster growth and higher incomes must be a major policy objective, the question is whether these come at the expense of higher income gaps within a country. As the Danish example highlights, this need not be the case. Income inequality in Denmark is considerably lower than it is in Israel. The Gini coefficient of disposable incomes (that is, after accounting for the deduction of taxes and the addition of welfare payments) is a full one-third lower in Denmark than in Israel. The share of Danish households living below the disposable income poverty line is 62 percent below the share in Israel, that is, Denmark has a poverty rate that is roughly one-third that of Israel.

The bottom line is that it is possible to have both much higher incomes and economic growth and much lower rates of income inequality and poverty. The question is how these twin outcomes might be accomplished, how the system of flexicurity is related to these differences in economic performance, and what aspects of the system might be applicable for Israel?

The primary question is whether flexicurity is a win-win (i.e., Pareto improving) set of policies in which both employers and workers end up better off, or is one group better off at the expense of the other (i.e., zero-sum game)? The fact that the Flexicurity countries have relatively high productivity, high living standards, and high employment rates is not an indication that flexicurity is a win-win because there is a serious absence of counterfactuals (or understanding of how the outcomes in Flexicurity countries would have been different if flexicurity were not the policy). In other words, the high government expenditures needed to fund flexicurity policies require higher taxes – or reduction of other expenditures – which reduces the incentive to invest and to work, which in turn reduce productivity and employment. So had there been lower taxes in the Flexicurity countries, could productivity and employment rates there have been even higher than they currently are? One of the primary difficulties in this realm is isolating the impact of flexicurity policies on socioeconomic outcomes. To our knowledge, there does not exist even one rigorous econometric study providing such an examination of statistically significant relationships, let alone causal links. Given the huge number of factors at play, it may not be too surprising that no such findings can be found.

In lieu of empirical research testing to examine whether flexicurity is a win-win, the second best approach then arises. Specifically, even if one could say that the Danes (for example) could have had even higher productivity and employment rates without flexicurity, the fact that they already have some of the highest rates could be considered sufficient in light of the perceived benefits resulting from the employment flexibility and personal security that they have.

The question is whether it might be possible to replicate the Danish example in Israel? To be able to better respond to this question, there is a need to understand the underlying reasons why these two countries have such differences in productivity and employment rates, as well as in wages and in income inequality. How much of these differences are structural (e.g., educational quality, quantity and disparity; physical infrastructure; competition) and how much are behavioral (e.g., formation and enforcement of laws, rules and regulations). The objective here is to examine the potential contributions and applicability of flexicurity policies in Israel.

2. *Defining Flexicurity*

Starting in the 1980s, the debate between hiring/firing flexibility sought by employers and employment protection legislation demanded by trade unions in Europe became louder. The strong economic performance of Anglo countries including the United States, Canada and the United Kingdom, as well as the "Dutch miracle" of the 1990s (a quick recovery from slow growth and high unemployment as a result of labor market reform), convinced some policy makers of the importance of deregulating labor markets. They believed that improved productivity, economic growth and a stronger labor market would ensue from employment flexibility. Simultaneously, labor groups expressed concern regarding workers' rights and financial security. The term flexicurity, a strategy to increase both flexibility within labor markets and individual security, emerged in the mid-1990s in the Netherlands (Tangian, 2008). Spotlight A describes the Dutch "Flexibility and Security Law" that represented a major milestone in the implementation of flexicurity policies in the Netherlands.

Spotlight A: **The Dutch Flexibility and Security Law**

The Dutch Flexibility and Security Law and accompanying legislation ("the Law"), enacted in the late 1990s, represented a monumental shift towards flexicurity via labor regulation in the Netherlands. Prior to the law, employers had to navigate a cumbersome process to receive permission from a regional employment office in order to dismiss a worker. By the mid-1990s many employers were circumventing this requirement by asking civil courts to dissolve employment contracts (Houwing, 2010).

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The Law simplified and sped up the procedures for dismissing regular employees and shortened the required notice period for dismissal. The Law also implemented the "3-3-3" rule for fixed-term contracts, allowing employers to hire a worker for up to three consecutive fixed-term contracts for a total of three years, at which point they were required to offer an open-ended contract. The Law considered contracts to be consecutive if they were renewed within three months, which prevented employers from indefinitely rehiring workers on limited term contracts and preventing them from obtaining the full benefits and security of regular employment. Simultaneously, in order to increase access to temporary workers, the Law also liberalized rules on temporary work agencies, removing their licensing requirement.

Various measures were implemented to improve security for non-regular employees, including: 1) the presumption that the relationship between employers and employees implies the existence of an employment contract for workers, subject to labor laws, even if one does not formally exist; 2) a guarantee of a minimum three hours pay when on-call workers are called to work; 3) a limit of a one-month trial period for contracts lasting up to two years; 4) coverage of temporary workers by a legal employment contract that allows for benefits such as pension and sick leave, albeit with more flexibility than a standard contract.

It is important to note, however, that the Law allows for deviation from these regulations through Collective Labor Agreements.

By the early 2000s, the concept of flexicurity had gained traction throughout Europe. It was defined as a policy that aimed to "enhance the flexibility of labor markets, work organization and labor relations on the one hand, and to enhance security – employment security and social security – notably for weaker groups in and outside the labor market, on the other hand" (Wilthagen and Tros, 2004).

Key elements of flexicurity, shown in Table 1 and communicated by the 2007 European Commission's "Towards Common Principles of Flexicurity," include: 1) flexible contractual arrangements in open, inclusive labor markets; 2) life-long learning and upgrading of skills; 3) active labor market policies; and, 4) a social welfare system that provides protection during transition periods.

The European Commission (2007) recognized that flexicurity must be adaptive to important cultural and socioeconomic differences among member countries. It also highlighted that the support of the social partners (labor unions and employer groups) was imperative for the advancement of flexicurity principles. The Commission articulated that flexicurity requires larger government budgets dedicated to supporting labor activation programs and providing financial assistance for the unemployed, with higher taxation levels likely to be required.

Table 1. **The four main principles of Flexicurity**

Flexibility			Security
Flexible and reliable work contracts in accordance with labor laws, collective wage bargaining agreements and modern work organization principles.	The introduction of lifelong learning strategies to support the continual adaptability of employees, particularly the most vulnerable in the labor market.	Effective active labor market policies, including counseling, assessment, training and wage-subsidized jobs.	Modernization of social security systems to provide financial support that encourages employment and facilitates labor market mobility.

Source: European Commission, 2007

The terms flexibility and security can be further broken down into various components, as shown in Table 2. While flexicurity policies have tended to focus on promoting external flexibility such as hiring and firing, there has been a more recent emphasis on internal flexibility (such as hours worked), functional flexibility (adjusting employee tasks to fit employer needs) and pay flexibility as well (basing compensation on merit and market conditions). The security aspect of these policies does not take the form of job security that ensures that an employee maintains the same job with the same employer. Instead, the emphasis is on increasing the likelihood of individuals remaining employable, ensuring sufficient income during transition and unemployment periods, and enabling individuals to better combine their work responsibilities with their family commitments.

Table 2. **Key elements of Flexicurity**

	Flexibility
External	Ease of adjusting number of workers, including hiring and firing (e.g., dismissal notice periods and procedures, required severance payments) and flexible contract forms
Internal	Ease of adjusting work intensity, including overtime, part-time, weekend work, or use of flexible working-time schemes
Functional	Ease of adjusting employee tasks to fit current needs, including job rotation, muti-tasking, increased employee autonomy and decision making responsibility
Pay	Ease of adjusting worker pay based on results, performance and the market
	Security
Employment	Heightened likelihood of remaining employable and being able to find work
Income	Heightened likelihood of receiving sufficient and consistent income in periods of transition or unemployment
Combination	Heightened likelihood that a person can combine work with private responsibilties and commitments, such as family

Source: Wilthagen and Tros, 2004

Aside from the advantages to employers, there are two notable benefits of flexibility for workers. One important goal of flexibility is to promote lifecycle transitions, helping individuals move more seamlessly through educational and training paths and various career positions. Flexibility is intended to encourage upward mobility along with talent and skill development, which also heighten employability.

Second, flexibility in the labor market for employees on regular, open-ended contracts is also intended to reduce labor market segmentation between regular and non-regular (temporary agency or fixed-term contract) workers.[1] Such labor market segmentation can lead to vast differences between the protection, rights and social security benefits of regular and non-regular employees. Where significant segmentation exists, workers can get trapped in a cycle of ongoing work relationships that exclude them from collective wage bargaining agreements, employee learning and investment, social security and other benefits (European Commission, 2007).

3. *Classification of Developed Countries by Flexicurity Parameters*

There have been many efforts to classify countries according to labor market and social policies, particularly within the flexicurity framework. Studies utilize a broad range of indicators that are aggregated and analyzed in various ways. Nonetheless, the results tend to be similar, with general consensus on five major country categories across the developed world. These categories are as follows:

- Anglo-Saxon countries (Australia, Canada, Ireland, New Zealand, UK, USA), characterized by high labor market flexibility, low security relative to Western European countries and low taxation
- Flexicurity countries (Denmark, Finland, the Netherlands, Norway, Sweden), defined by high security, medium labor market flexibility and high taxation

[1] Temporary workers are those workers who are paid through an employment agency/labor firm. Fixed-term contracts entail those employees working on a contract of fixed duration and excludes employees paid by an employment agency/labor firm.

- Continental countries (Austria, Belgium, France, Germany), characterized by relatively low labor market flexibility, medium-to-high security and relatively high taxation
- Mediterranean countries (Greece, Italy, Portugal, Spain), considered to have fairly rigid labor markets with lower security than Western European countries and mixed patterns of taxation
- Eastern European countries (Czech Republic, Estonia, Hungary, Poland, Slovakia), characterized by low security, medium flexibility and relatively low taxation

Both the Anglo-Saxon and the Flexicurity countries have historically had high rates of labor market participation and relatively low unemployment. The Flexicurity model, with medium levels of flexibility, places a considerable emphasis on lifelong learning, vocational training and labor activation policies. Over the long term, it has enjoyed strong innovation and productivity outcomes, good working conditions (based on high marks from employees on job satisfaction and work-life balance) and particularly low rates of poverty and income inequality. The Anglo-Saxon model is notable for its high external flexibility (including high labor mobility and low labor market segmentation). It is characterized by high rates of secondary education coupled with moderate levels of vocational training and little investment in labor activation. The model thus entails lower taxes and lower budget spending on transfers than in the Flexicurity countries (European Commission, 2007).

Nonetheless, given historical, cultural and major socioeconomic differences among the countries analyzed, it is challenging to attribute specific social and economic results solely to labor flexibility and labor activation or to income security policies. As described in Spotlight B, the Great Recession in recent years has also played out differently across the different systems.

Spotlight B: **Flexicurity and the Great Recession**

The severe recession beginning in 2008 affected different European countries in different ways. With a very low unemployment rate prior to the crisis, Denmark witnessed a relatively large increase in unemployment between 2007 and 2009. Germany was an anomaly during the crisis and saw unemployment rates decrease. The German response to the crisis entailed a reliance on internal flexibility, with almost one-third of firms implementing reduced work hours, rather than a reduction in workers. With the exception of high crisis countries such as Portugal and Spain, those countries with stricter employment protection legislation, such as Austria and Belgium, tended to reduce work hours rather than the number of employees during the recession. Nonetheless, because of greater job creation and destruction in higher flexibility labor markets, the number of unemployed tended to be higher but the duration shorter in Flexicurity model countries (Andersen, 2011; Schmitt, 2011).

The outgoing head of the Danish Federation of Trade Unions noted (Bredgaard and Daemmrich, 2013): “When I was young, security meant having a good, solid job. This was not very exciting – but in a way, it was very safe. This security disappeared as globalization emerged. Security is no longer to hold on desperately to the same job throughout your life. Security is to stay cool when you hear rumors of outsourcing from the boardroom. Because deep down you know that you have solid skills and that you will quickly be able to find a new job if the old one is relocated. Security is not to be able to stay on. Security is to be able to move. It is precisely this new security through training and education that we have now embarked on creating for every worker.”

4. *Flexicurity Countries Compared to Others*

A comparison of the five country groupings described above, together with Israel, on a number of indicators relating to flexibility, security and the labor market is provided in Appendix Table 1. Labor market flexibility is assessed using OECD employment protection legislation indices for regular workers (those with open-ended contracts) and for those workers with temporary contracts, including both workers hired through temporary work agencies and with fixed-term contracts. The index for regular workers considers expenses and procedures incurred in dismissing an individual or group of workers with typical open-ended contracts. A higher index score indicates a more rigid labor market where it is harder to hire and dismiss workers.

Israel scores relatively low on the Employment Protection Legislation Index. While not as flexible as the Anglo-Saxon countries (for example, Israel has particularly high mandatory severance pay requirements), it has short notification periods and low procedural barriers for individual dismissal. Dismissal of a larger number of workers entails an additional notification requirement to the Israeli Employment Service Bureau, but unlike many other OECD countries, this does not involve additional costs (OECD, 2013a).

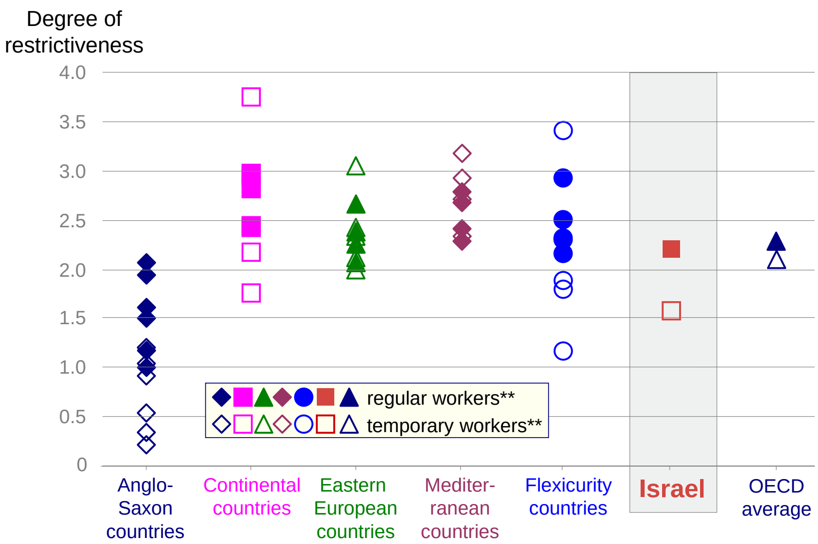
Using the Employment Protection Legislation Indices, Figure 2 provides a visualization of Israel relative to the various country groupings with regard to employer hiring flexibility. It shows the spread within the country groupings for both regular workers (those with open-ended contracts) and workers with temporary or fixed-term contracts.

While Israel appears to be quite similar to the OECD average with regard to regular workers – and more flexible for temporary/fixed-term contract workers – such a comparison blurs the picture somewhat because averages do not show the differences between different country groupings. The Index ranges for regular workers are fairly similar for the various European groupings and Mediterranean countries while the Anglo-Saxon nations have considerably greater hiring and firing flexibility for such workers. Israel is situated between the Anglo-Saxon group and the other groups, with less flexibility than the Anglo-Saxon countries and greater flexibility than the other groups.

Figure 2

Hiring *flexibility* for employers

Employment Protection Legislation Index*, 2013



* The OECD's Employment Protection Legislation Index ranges from 0 (the least restrictive) to 6 (the most restrictive).

** The index for regular workers measures how strict regulations are for employers to dismiss workers with open-ended contracts. The index for temporary contracts measures how strict the regulations are on the use of temporary or fixed-term contract workers.

Source: Dan Ben-David and Liora Bowers, Taub Center

Data: OECD

With regard to temporary/fixed-term contract workers, there is greater within-group variation, although the position of the various groups relative to others remains unchanged. Here, too, Israel's employers have greater flexibility with respect to nearly all of the European countries, but less hiring flexibility than all of the Anglo-Saxon ones.

Like the Anglo-Saxon countries and several others, Israel does not limit the types of work that can be done by temporary workers. However, Israel's authorization and reporting requirements on temporary work, as well as limits on the number of renewals of temporary worker assignments, are considered of medium strictness. When it comes to the fixed-term contracts, Israel is again aligned with the Anglo-Saxon countries. There are no significant restrictions on what circumstances or for what type of work fixed-term contracts can be used, nor the duration or number of such contracts an employer can sign with an employee (OECD, 2013a). It is important to note, however, that Israel's public sector is much less flexible than either the private sector in Israel or the public sectors in the Flexicurity and Anglo-Saxon countries. (See Spotlight C for more details).

Spotlight C: External Flexibility in the Public Sector

Although the public sector is an important part of the overall work force in Western countries, the flexicurity discussion largely focuses on the private sector. The public sector across countries tends to be less externally flexible than the private sector, and focuses more on internal mobility within the government.

Nonetheless, there does appear to be some correlation between external flexibility in the private and public sectors. For example, the Flexicurity

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countries have a public sector that is considered a “position-based” system, characterized by hiring based on openings for specific positions that are broadly accessible to both internal and external candidates.

Such a system shows greater mobility between the public and private sectors, and greater managerial flexibility and delegation, as agencies often determine their own human resource management rules and employees’ rights are more aligned with their individual performance (Kuperus and Rode, 2010). With the exception of Ireland, the Anglo-Saxon countries also tend to be more position-based systems (OECD, 2014).

The public sector in Israel operates mainly as a career-based system, characterized by specific entry criteria that are decided centrally rather than at the managerial/departmental level, and continuous career development and job protection that supports lifelong civil service employment. This structure is reminiscent of the systems in the Continental countries.

The OECD Recruitment Index that ranges from 0 (an externally less flexible system) to 1 (a more externally flexible system) takes into account the entry mechanisms, external recruitment methods, and selection processes of senior civil servants. This index gives Israel a score of 0.35, well below the OECD average of 0.5 on this index, reflecting a less flexible and more career-based system (OECD, 2014). The Israeli public sector employs about 19 percent of the labor force, slightly above the OECD average but much lower than the 28 percent average of the Flexicurity countries (Central Bureau of Statistics, 2013).

There is far less external flexibility in Israel’s public sector than the private sector. A 2013 report by the Civil Service Reform Commission identified the lack of performance evaluations in determining advancement or pay together with little turnover among managers and lengthy hiring periods as key problems in the civil service (Dayan, 2013; Bassok, 2013).

Panels A-C in Figure 3 provide comparisons of the security picture for employees – where it is important to remember that this refers to national safety net attributes rather than to job security in a particular place of employment. Panel A displays the share of unemployed persons receiving unemployment benefits. Israel places quite a bit below the OECD average, and below all but two of the countries in the figure, with only 27 percent of the unemployed in Israel actually receiving unemployment benefits (International Labor Organization, 2011). One of the reasons for this is that many of Israel's longer-term unemployed have exhausted their benefits, which cover a relatively short period of time. Others may not receive such benefits because they are new entrants to the labor market or because they recently entered the labor market and did not accumulate sufficient working days to meet the requirements for benefits.

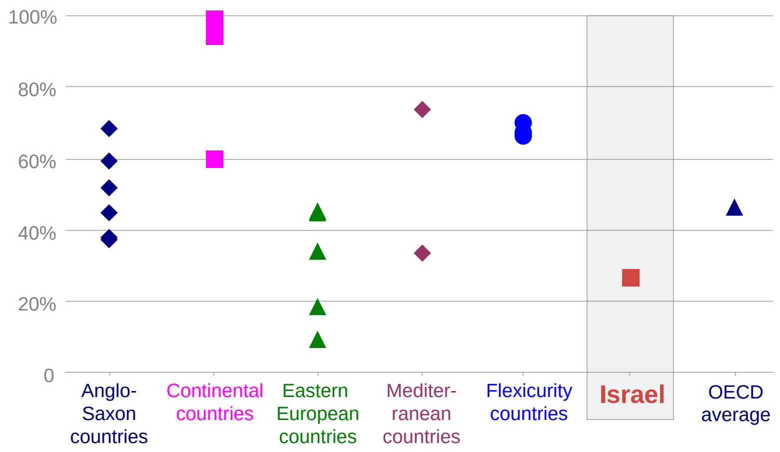
In 2011, Israel spent only 0.6 percent of its GDP on unemployment insurance and income support for the unemployed, which is among the lowest OECD outlays in this regard. The low spending, however, may be a positive indicator partly related to Israel's low unemployment rate. Consequently, it should come as no surprise that Israel's net income replacement rate (the amount that the unemployed receive as a percent of their disposable income – i.e., after taxes and transfers – during their previous employment) is also relatively low (Panel B). On average, considering various earnings levels and family situations, an adult in Israel can expect to have a net replacement rate of 41 percent via unemployment and social support programs in the five years following unemployment. This is among the lowest income replacement rates in the OECD. It is important to note, however, that individuals' personal situations greatly affect their replacement rates. For example, Israelis who are married with children tend to have replacement rates that are closer to the OECD average. Furthermore, initial replacement rates for those who lose their job in Israel are actually quite high relative to the OECD, but the financial support does not last very long.

Finally, active labor market policies, which include job placement, training and job creation policies, are important for both flexibility and security of the work force. These programs are designed to help workers develop new skills, retrain or connect with open job opportunities. Countries often make participation in such programs mandatory in order to receive unemployment benefits which also serves as a motivator to counter the disincentives to work that come from receiving income support. As shown in Panel C of Figure 3, active labor market policies are used extensively in the Flexicurity countries, which spend an average 1.37 percent of their GDP on these efforts. At 0.18 percent of GDP, Israel spends well below the OECD average on such programs and is situated at the bottom end of all of the countries in the figure.

Figure 3 (continued on next page)

***Security* for employees**

Panel A: Share of unemployed receiving unemployment benefits, 2006-2008*



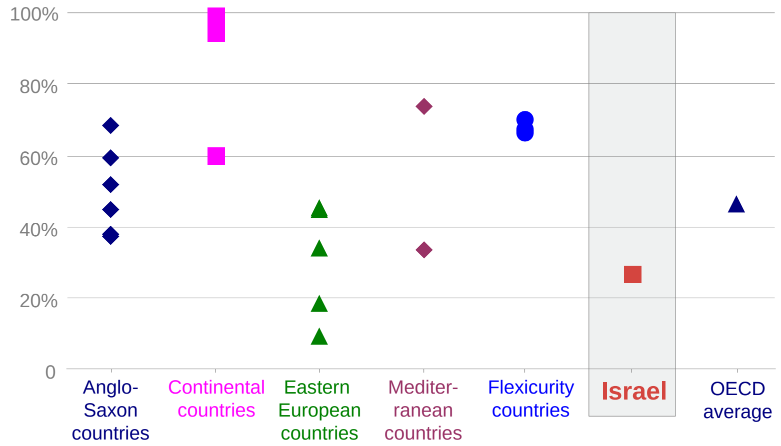
* Data not available for select countries

Source: Dan Ben-David and Liora Bowers, Taub Center
Data: International Labor Organization (2011)

Figure 3 (continued from previous page)

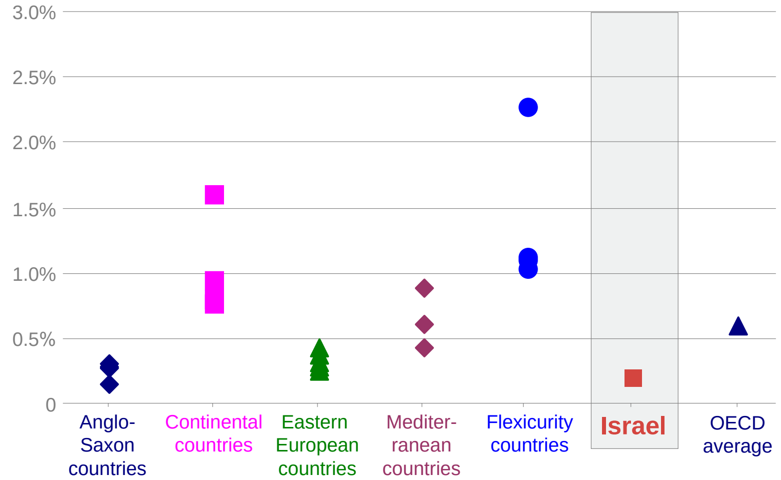
***Security* for employees**

Panel B: Net income replacement rate for unemployed*, 2011



* Data not available for select countries

Panel C: Expenditures on active labor market policies as percent of GDP**, 2011



* Net income replacement rate as percent of previous income earned (after taxes and transfers); averaged across various wage rates and family situations; includes social support and other means-tested benefits; average of first 60 months following unemployment

** Active labor market policies include job placement, training and job creation policies. Data not available for select countries.

Source for both: Dan Ben-David and Liora Bowers, Taub Center

Data for both: OECD

To sustain large government support in labor and other welfare policies, taxation levels are much higher in the Flexicurity countries – averaging 43 percent of GDP versus 29 percent and 33 percent of GDP in the Anglo-Saxon countries and Israel, respectively. In order to sustain the flexicurity model of a substantial, generous safety-net, the model relies on a high rate of employment. As Appendix Table 1 shows, Flexicurity countries have higher labor force participation and lower unemployment rates among working-age adults than the other four country groupings. Israel also has relatively low unemployment rates, but its labor force participation rate is around the OECD average.

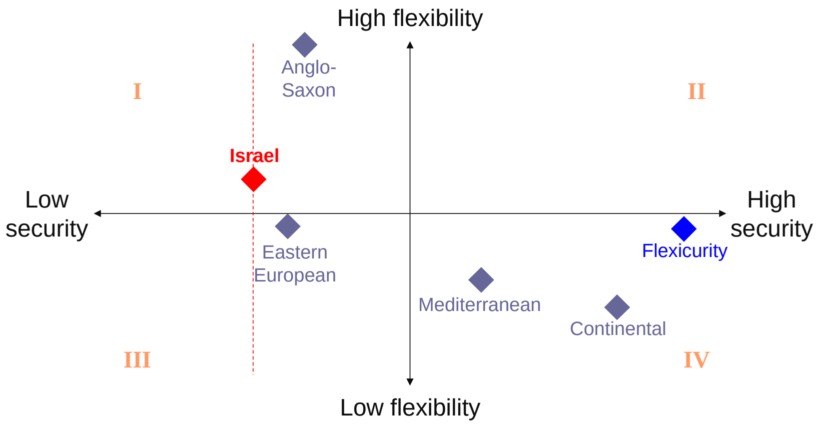
While Appendix Table 1 provides the country group averages – together with Israel's scores – on various measures of employment flexibility and security, Figure 4 merges a number of relevant indicators to create a composite index showing the relative positioning of the five country groups and Israel with regards to flexibility and security. The figure highlights Israel's unique position, characterized by a somewhat higher level of flexibility (slightly higher than the Flexicurity country average as indicated by its position on the vertical axis), but a low security level, even in comparison to the Eastern European and Anglo-Saxon countries (its location on the horizontal axis).

The picture that arises from the figure is not complete, since it shows the extent of the national safety net (in terms of provision of financial security and employability for individuals) in all of the sectors, while Israel's private and public sectors are distinguished by varying degrees of labor market flexibility within each of them. In other words, the private and public sectors in Israel are arrayed along the red dotted line in Figure 4 and the challenge that the country faces is how to move the entire dotted line rightwards and upwards in the direction of greater security together with greater flexibility (i.e., shortening the dotted line and moving it from Quadrants I and III to Quadrant II in Figure 4).

Figure 4

Classification of countries

by degree of employment flexibility and security*, various years



* Security and flexibility are measured relative to OECD averages based on the two flexibility indices (Employment Protection Legislation Indices for regular workers and for temporary workers) and four security indicators (active labor market spending, net income replacement rate, unemployment insurance spending, and percent receiving unemployment benefits).

Source: Dan Ben-David and Liora Bowers, Taub Center
Data: OECD

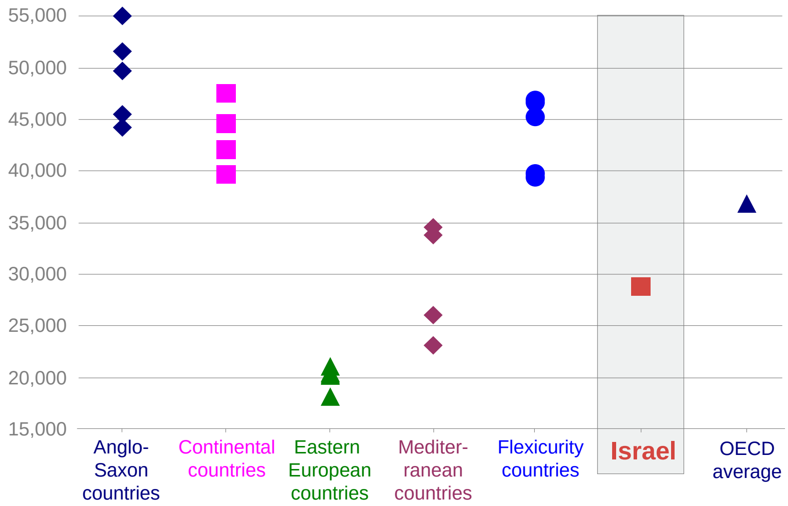
5. A Comparison of Macroeconomic Performance Between Flexicurity Countries and Other Countries

To what extent are the countries that are characterized by the different policies described above distinguished in their relative macroeconomic performances and are the various country groupings also distinguishable in this regard? Do the Flexicurity countries stand out in terms of macroeconomic outcomes? While the following analysis should not be considered as suggestive of causal effects of the policies, it is nonetheless useful in determining the degree of delineation between the groups, where this exists, while providing a basis for comparison to Israel.

Wages and labor productivity in Flexicurity countries are high and similar to Continental and Anglo-Saxon countries. The position of the wage range in the Anglo-Saxon countries is the highest, with wage ranges in all three of the groups positioned above the OECD average (Figure 5). Wages in the Eastern European and Mediterranean countries are all below the OECD average, with the former group below the rest. The average annual wage in Israel is below the OECD average and, in fact, below nearly all of the Western countries in Figure 5.

Figure 5

Average annual wages*, 2012



* In PPP dollars

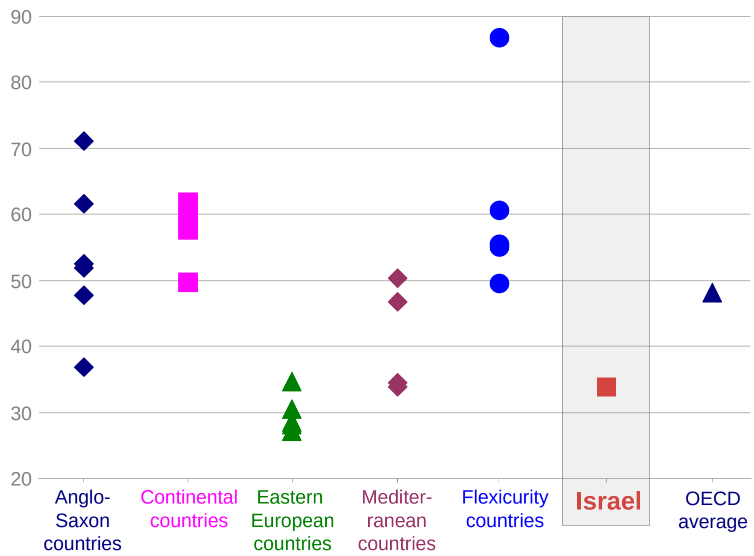
Source: Dan Ben-David and Liora Bowers, Taub Center
Data: OECD

The productivity picture is similar to that of the wages (Figure 6), although the spread between the countries is a bit greater. While the data underlying Figure 6 is the most recent available at the time of this writing, it is nonetheless susceptible to the fact that many of these countries have still not emerged from their worst recession since the 1930s. To enable a broader, long-run perspective of the country groupings' relative positions over time, Figure 7 (and Appendix Figures 1-4) provides data on these groups extending as far back as possible for each of the variables examined below.

Figure 6

Labor productivity

GDP per hour worked*, 2012



* In PPP dollars

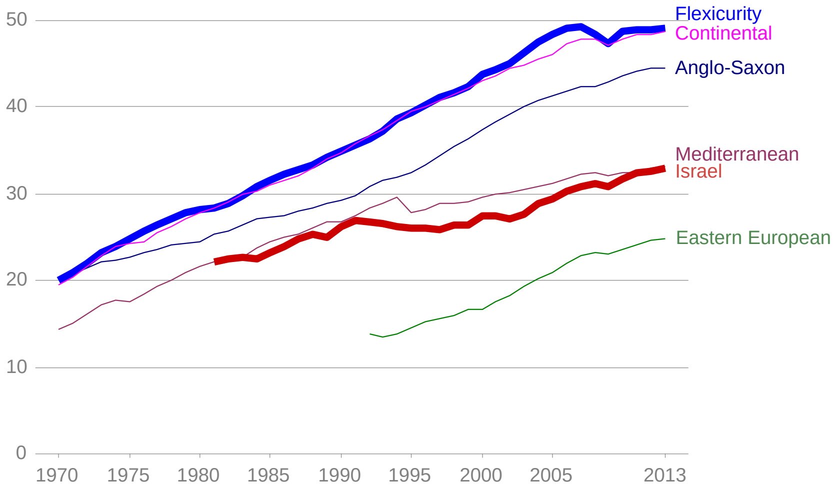
Source: Dan Ben-David and Liora Bowers, Taub Center
Data: OECD

The long-run labor productivity trends in Figure 7 show that the relative productivity levels of the groups to one another have been fairly consistent for decades. Productivity levels in the Flexicurity and Continental European countries were similar to the Anglo-Saxon countries in 1970. Since then, the productivity of the two former groups has risen steadily above the latter group, with nearly identical productivity levels between them for over four decades. After exhibiting slower productivity growth until the early 1990s, the Anglo-Saxon countries returned to a growth path that was roughly parallel with the Flexicurity and Continental European countries – albeit below them.

Figure 7

Labor productivity

GDP per hour worked*, 1970-2013



* In 2005 PPP dollars

Source: Dan Ben-David and Liora Bowers, Taub Center
Data: OECD

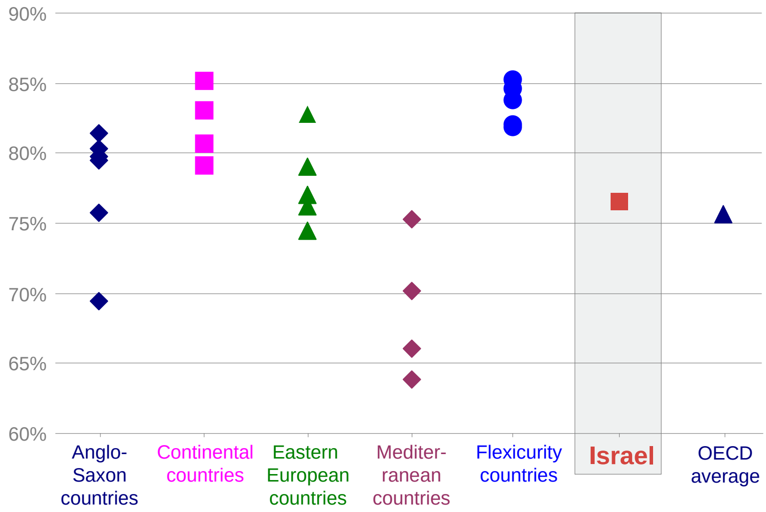
Israel's productivity path has been similar to that of the Mediterranean countries since 1980, although slightly below those countries for most of this period. These paths are not only at lower productivity levels than the Flexicurity, Continental and Anglo-Saxon groups, they are also flatter (with the exception of the recent major recession years), indicating that the Mediterranean countries and Israel have been falling further and further behind the leading developed countries for decades.

Employment rates of 25-54-year-olds are high and similar among the Flexicurity countries – and they are relatively comparable to rates of employment in the Continental European countries (Figure 8).

Figure 8

Employment rates

25-54-year-olds, 2012



Source: Dan Ben-David and Liora Bowers, Taub Center
Data: OECD

Employment rates in Eastern European and Anglo-Saxon countries tend to be lower than in the Flexicurity and Continental European countries, with the Mediterranean countries exhibiting the lowest rates among the groups. Israel’s employment rate in 2012 was slightly above the OECD average for this age group, though it is clear that this apparent resemblance to the OECD is simply a facet of averaging across relatively different country groupings. Israel’s employment rate is below the rates in all of the Flexicurity and Continental countries and above all of the Mediterranean countries.

As shown in Appendix Figure 1, the Flexicurity countries have consistently had the highest employment rates among all of the groups since the early 1980s, with the Continental countries steadily catching up to them together with the Anglo-Saxon countries. However, the severe recession of the past half-decade had a major negative impact on the Anglo-Saxon countries, causing their employment rates to drop considerably in recent years. Israel’s employment rates have consistently been at the bottom, together with the Mediterranean countries, until the onset of Israel’s major recession at the beginning of the last decade. After falling behind initially, Israel’s post-2002 recession recovery period led to employment increases while the recent Great Recession in the West coincided with a sharp drop in Mediterranean country employment to below Israeli levels.

Cross-country comparisons of income inequality (Figure 9) and poverty (Figure 10) are fairly similar, with the Flexicurity and Continental European countries displaying the lowest rates and the Eastern European countries not far behind them. Anglo-Saxon and Mediterranean countries exhibit substantially higher rates of inequality and poverty. In both instances, Israel is characterized by greater inequality and poverty than all of the other countries except the United States. The relative positions of these different country groupings – and Israel’s – have been fairly steady since the mid-1980s (Appendix Figures 2 and 3).

Figure 9

Income inequality, 2010

Gini Index of disposable incomes among working age population: ages 18-65

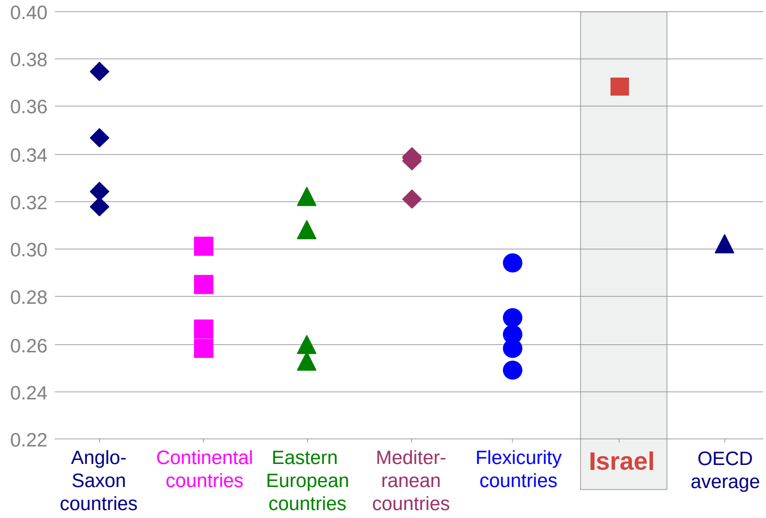
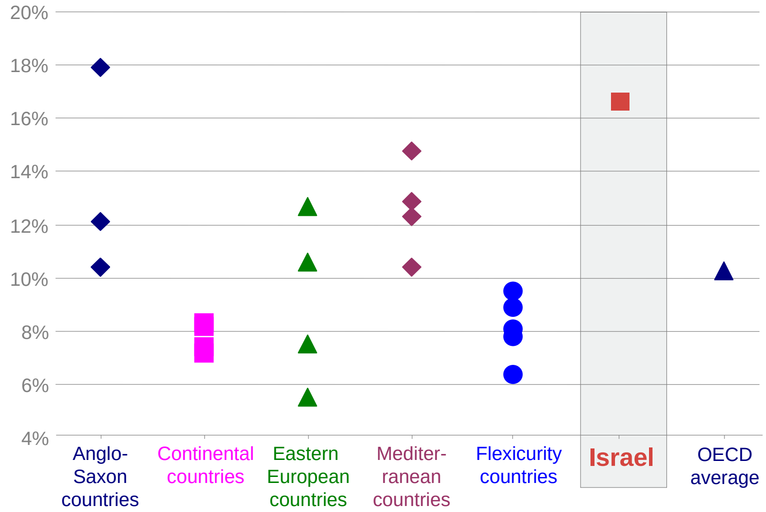


Figure 10

Poverty rates*, 2010

in disposable income for 18-65 age group



* Poverty line is 50 percent of median income

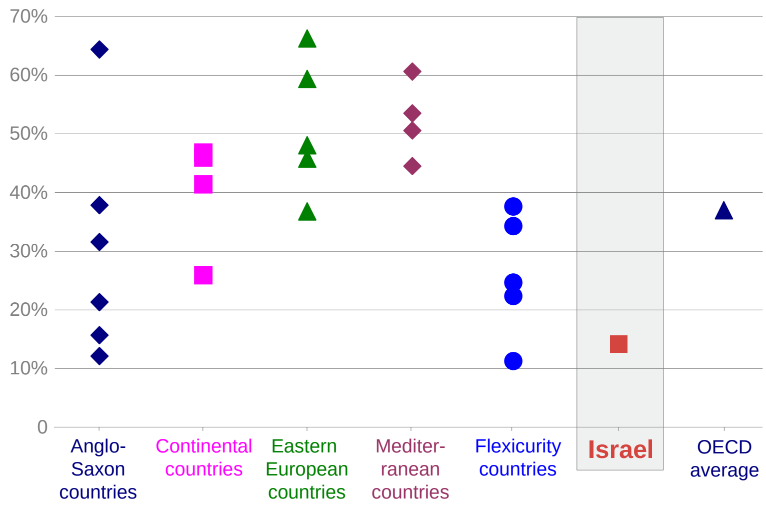
Source for both: Dan Ben-David and Liora Bowers, Taub Center
Data for both: OECD

The duration of periods of unemployment within a country provides an indication of, among other things, the generosity of the unemployment compensation on the one hand, and the ability to find employment and the flexibility of employers to hire and fire as needed, on the other hand. The share of unemployed persons in the Flexicurity countries who remained unemployed for less than one year is among the highest in the developed world. The flip side of this is that the share of unemployed persons in these countries who were unemployed for one year or more is among the lowest (Figure 11), a finding that is both interesting and instructive.

Figure 11

Percent unemployed for 1 year or more, 2012

as share of total unemployed, 25-54-year-olds



Source: Dan Ben-David and Liora Bowers, Taub Center
Data: OECD

The fact that this trend in the Flexicurity countries has been fairly consistent over the past two decades (Appendix Figure 4) makes it easier to understand the degree of worker satisfaction with flexicurity in these countries. They are given many months to do what is needed to find employment, while benefitting from relatively high unemployment compensation together with active labor market policies encouraging employment skills training to help them turn things around. The fact that the picture is reversed for unemployment duration lasting one year and over, and the fact that employment rates in Flexicurity countries are consistently very high in any event, is an indication that these policies – generous as they may be – are not open -ended.

Israel, as indicated previously, does not stand out in terms of the generosity of its unemployment assistance package and has relatively high flexibility for employers. As such, the percent of those unemployed less than one year in Israel is above the OECD average while the share of unemployed one year and over is among the lowest in the developed world since the mid-1990s (Appendix Figure 4).

The above indicators suggest some fairly substantial socioeconomic success among Flexicurity countries. Productivity and employment rates are high in these countries while rates of poverty and income inequality are relatively low. As noted before, it is hard to determine the specific contribution of flexicurity policies to the outcomes – particularly in view of the fact that non-flexicurity Continental European countries often display similar socioeconomic outcomes. That said, it is still noteworthy that it is possible to adopt successful policies that both encourage growth and provide security for employees, not in terms of protected employment in the same position but rather in the sense of a strong social safety net and labor activation programs that will catch those who fall and help put them back on their feet within the span of a year.

6. *Moving Towards a Flexicurity Model in Israel: Considerations and Recommendations*

The underlying system of labor relations is considered a key contributor to the socioeconomic success of flexicurity. Denmark has almost 70 percent union membership among employees, one of the highest rates in the OECD, with the vast majority of employees covered by collective bargaining agreements. Instead of focusing on employment protection, though, Danish unions have used their strong influence to improve working conditions, wages and training and are supportive partners to Danish flexicurity (Mailand, 2009).

The near universal representation of workers and employers in unions and employer associations, respectively, allows these groups to transcend narrow, particularistic demands and focus on collective needs. This has contributed to what might be considered a sense of social responsibility for the overall well-being of the country, even to the point that unions exert a moderating effect on wage increases. There is an emphasis on increasing productivity and efficiency with the belief that both employers and workers will benefit from these.

In Israel, roughly 65-75 percent of the work force is in the private sector, which is generally characterized by low employment protection for regular and temporary workers,[2] while the remainder of the country's work force are in the public sector that is characterized by very little or no flexibility. Among workers who have little employment protection, the required notification period for termination of employment is relatively short and the procedural barriers to employment termination are also low. Aside from notification requirements, there are next to no additional costs incurred in the dismissal of larger groups of workers. In the case of temporary workers, there is no limit on types of work, with some reporting requirements and limits on the renewals of temporary work

[2] This is not always the case, with the banking sector being one major exception.

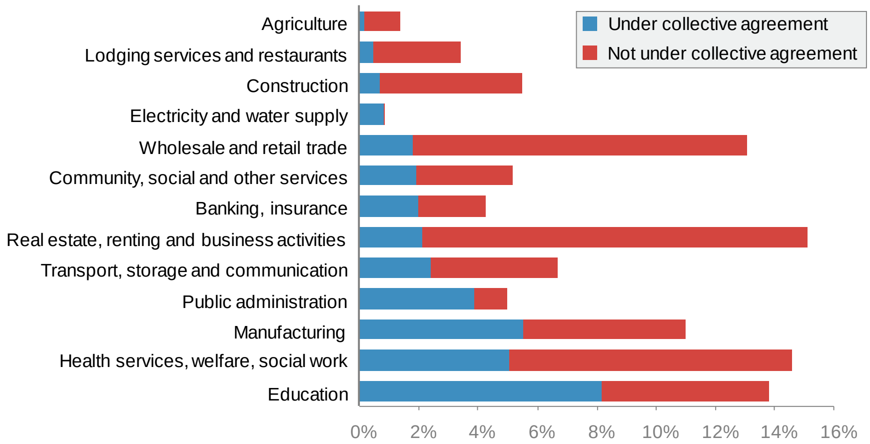
assignments. There is no restriction on the number of renewals for fixed-term contracts.

Figure 12 shows the share of Israeli workers in each economic sector. These shares are further divided by the proportion covered under collective bargaining agreements and the remainder who are not covered. It is important to note that the collective agreement coverage data shown here is self-reported, while in practice it is assumed that this rate is slightly higher as not all individuals are aware of their coverage status. Sectors with high levels of job protection are public administration; water and electricity; education, health and social services; finance; community services; transportation and communications; and portions of manufacturing.

Figure 12

Distribution of workers by economic sector and collective agreement coverage rates in Israel*

2011 (distribution of workers) and 2012 (coverage rates)



* Distribution of the labor market represents Israelis aged 25-64. Collective coverage rates are based on 2012 self-reported data, and all together represent about one-third of workers. However, experts in the field estimate that actual collective agreement coverage rates are closer to 50 percent.

Source: Dan Ben-David, Liora Bowers and Kyrill Shraberman, Taub Center
Data: OECD, International Labor Organization

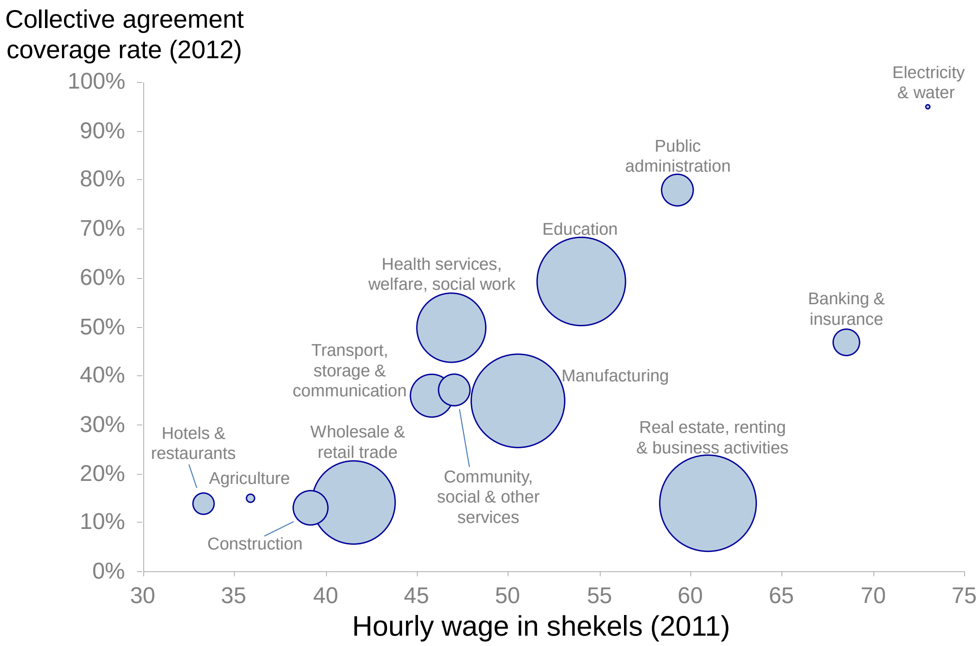
As noted in the discussion on Figure 4, Israel's private and public sectors are arrayed along the dotted red line extending from Quadrant I to Quadrant III with varying degrees of flexibility. One possible proxy for flexibility is the rate of collective agreement coverage detailed in Figure 12. The positive relationship between this coverage rate and hourly wages can be seen in Figure 13 (the sizes of the various sectors are depicted by the size of the circles in the figure). On the lower left side of the figure, with the lowest rates of collective agreement coverage and lowest average hourly wages are workers in hotels and restaurants. Close by are the agriculture and construction sectors with low coverage rates and low hourly wages. At the top far right of the figure are the electricity and water workers. This sector comprises a relatively small number of workers; nearly all are covered by collective agreements and their average wages are the highest of all the sectors.

While the positive link between collective agreement coverage and hourly wages appears to be quite strong, this relationship should nonetheless be qualified. For example, hourly wages are also linked to education levels and there tends to be a positive relationship – albeit a somewhat weaker one than in Figure 13 – between number of years of education and coverage rates as well as between the share of academics in each sector and coverage rates. On the other hand, it is not obvious that this link is due to higher productivity, since Israeli collective bargaining agreements invariably contain clauses providing for higher wages to individuals with academic degrees regardless of whether the academic education is even related to their work and actually increases productivity.

Figure 13

Collective agreement coverage rates* and hourly wages

hourly wage, distribution of workers and coverage rates, by economic sector



* Collective coverage rates are based on 2012 self-reported data, and all together represent about one-third of workers. However, experts in the field estimate that actual collective agreement coverage rates are closer to 50 percent. Size of bubble represents relative size of the sector by share of 25-64-year-old employees.

Source: Dan Ben-David, Liora Bowers and Kyrill Shraberman, Taub Center

Data: Central Bureau of Statistics (2011), Bank of Israel (2012)

An estimated 50 percent of Israeli employees are covered by collective agreements. Of these, it is estimated that 50-70 percent are more difficult to dismiss (to varying degrees). The remainder (i.e., those covered by collective agreements but who are still relatively easy to dismiss) include some specific groups such as privatized social workers, temporary workers, security guards, etc. In general, Israeli collective agreements include provisions for tenure. While on paper it is not so difficult to dismiss individuals with tenure, there are nonetheless barriers to dismissal in the form of work place norms, practices and worker committees.[3]

Moving Israel towards a flexicurity model entails various benefits as well as challenges. Flexicurity's promise of a dynamic, competitive and adaptable labor market could greatly benefit Israel in the many sectors that are quite the opposite. It would be highly beneficial to implement policies that would improve the country's competitiveness, including substantially spurring its currently low labor productivity. Improvements in the social welfare system that would be reflected in lower rates of poverty and income inequality are particularly essential given Israel's weak performance in this area, although there is concern about the possible adverse effects on employment if these changes are not part of a comprehensive policy.

Another benefit of a flexicurity model is the promotion of broad participation in the labor market, including among women and older adults. As Israel seeks to address its rapidly aging population (it is currently relatively young, but its rate of aging is relatively high) and increase employment rates among the 55+ age group, lifelong training and skills adaptation, along with working hours flexibility, can help attain this goal.

A major concern regarding the active pursuit of flexicurity policies relates to the feasibility of truly replicating the Flexicurity model. Many European governments attempting to introduce labor reforms have faced significant challenges and social turmoil. Consequently, the current thinking is that countries such as the Netherlands and Denmark that have been more effective in these areas likely enjoyed particularly supportive historical circumstances. In fact, it has been argued that the Danish model

[3] Information and estimates in this paragraph were provided by Guy Mundlak, Tel Aviv University.

is not the result of carefully crafted policies around a long-term strategy, but rather, the result of historical processes with roots in the late 1800s and mid-1900s' institutional structure and social agreements over time (Zhou, 2007). Since an historic agreement in 1899, collective bargaining rather than the courts or government has been the main platform for dispute resolution between employers and employees in Denmark. Danish unions accepted the right of employers to hire and fire as needed, in exchange for employers accepting organized labor's right to negotiate and strike on issues related to wages, benefits and working conditions.

External flexibility, alongside an emphasis on improved working conditions, has thus been a long-standing feature of the Danish system of employer-union relations (Bredgaard and Daemmrich, 2013). Danish trade unions also chose not to fight against the growing globalization or free trade of the 1990s, but pushed harder for continued training and education for both employed and unemployed workers. A 2005 Eurobarometer survey showed that 70 percent of Danes agreed that it is "good for people to change jobs every few years," while less than 30 percent of their German or Austrian counterparts felt the same way. Danes likewise were twice as likely as the average European to view the impact of globalization on domestic companies and job growth as positive (Bredgaard and Daemmrich, 2013).

An influential study by Algan and Cahuc (2006) showed much higher rates of public spiritedness – that is, people believing it is wrong to claim government benefits to which one does not have a right – in Flexicurity countries versus other developed countries. This study argues that countries with weak public spiritedness would have a hard time implementing flexicurity policies that may further incentivize people to take advantage of government benefits.

In Israel, various incentives exist for non-participation in the labor market, such as universal child allowances and benefits given to Haredim (ultra-Orthodox Jews) studying in a yeshiva. Long-lasting incentives towards non-participation in the labor force alongside potentially lower levels of public spiritedness (as evidenced by the Israel's very large shadow economy – see Gruber, 2014) may challenge attempts to develop an effective flexicurity system. In light of its historical evolution, both in terms of employer-employee relations and the welfare state compared to the Flexicurity countries, it is unclear whether Israel would be able to effectively replicate the various components of flexicurity. Furthermore, flexicurity itself was never a deliberate policy package in the countries where it exists. Instead, it culminated from evolution of employee-employer relations, alongside supportive legislation.

Just as important is the ongoing debate about the sustainability and perseverance of flexicurity under difficult economic times. As the socioeconomic indicators examined in this chapter suggest, it does not appear that the Flexicurity countries fared worse than other developed Western European countries during the massive recession of recent years. If anything, they appear to have done better in some instances. Nonetheless, large increases in unemployment during the Great Recession increased budgetary spending as a result of rising unemployment and social support costs, challenging the quality and resources of labor activation programs (Andersen, 2011). That said, while business cycles exist and must be accounted for, Israel must design its policies on the basis of a long-term perspective. In moving forward with a flexicurity approach, the following recommendations are important for policy makers and the general public in Israel to consider:

1. The Flexicurity model requires significant budgetary expenditures in both income security measures and labor activation policies. For Israel, this means much greater expenditure on welfare alongside the initiation of new labor activation programs, such as a revamped “Wisconsin program” meant to train and connect the unemployed with new opportunities. Ensuring the continued availability of childcare, which is relatively accessible in Israel – and growing with the expansion of universal preschool starting at age three – is an important contributor to labor market participation.

2. The Flexicurity model involves high levels of direct taxation and its generous income support benefits create adverse incentives for

prompt re-entry into the labor market. Denmark counters these disincentives with labor activation policies and monitoring systems to ensure continued employment search by the unemployed. For example, in certain cases, unemployed Danes are required to accept job offers outside of their primary occupation after three months of unemployment benefits, and failure to be activated (e.g., refusing employment or not participating in training programs) results in benefit loss (Zhou, 2007). The impact of these measures was shown previously in Figure 11, where among the unemployed, Denmark (and the other Flexicurity countries) has a relatively high share that are unemployed for a period of less than one year, but relatively low unemployment duration for one year and over. In Israel, policies such as a more substantial negative income tax could help provide incentives to work. Improved enforcement of existing labor laws (notably on minimum wage, working hours and discrimination) is imperative to encourage labor market participation by and provide security for lower-skilled workers.

3. The obligation of the government, employers and individuals to lifelong learning is a core principle of the flexicurity system. Employment contracts stipulating continued learning, and government-supported career guidance, training and education opportunities are an important policy response to increased job insecurity (Sultana, 2012). For example, employers and unions in Denmark are very involved in designing and participating in continuing vocational training, which is largely financed by the government (Bredgaard and Larsen, 2007). Almost a third of Danish working-age adults participated in education and training in 2011, a high rate among European countries, approached only by Finland and Sweden (Eurostat, 2011). Employers provide the time, as collective agreements generally grant employees the right to take 1-2 weeks off with pay in order to participate (Jørgensen, 2009). Developing supportive cultural attitudes and

implementing policies at the government and employer level that promote lifelong learning are essential for creating a robust flexicurity system in Israel.

4. Israel already has relatively low employment protection for non-regular workers, particularly those on fixed-term contracts. There is concern that increasing flexibility "at the margins" would increase segmentation and cement gaps between regular and non-regular workers, particularly hurting women and minorities. Emphasis on flexibility within Israeli labor markets should thus focus on regular workers, particularly increasing the flexibility within organizations in areas such as work hours, schedules and tasks.

5. Israel stands out from the Flexicurity and Anglo-Saxon countries with regard to having particularly low external flexibility in the public sector relative to the private sector. To move towards the Flexicurity model entails a shift away from career-based to position-based public sector employment. This requires more flexibility in hiring and firing, the hiring of individuals on the basis of credentials and merit for specific positions, and greater mobility between the private and public sector. It also requires decentralization and delegation of work on the basis of performance results.

The bottom line is that much of Israel's private sector already has considerable employer flexibility, so it is unclear what could be given to these employers to encourage them to support a stronger safety net and lifelong learning for employees. On the other hand, there are some sectors – private as well as public – in which employees have so much job protection (i.e., low employer flexibility) that there appears to be little incentive for them to give up this job protection in order to provide employers with more flexibility. In light of both of these obstacles, it appears that the primary areas that Israel needs to concentrate on are:

- The enhancement of labor productivity – which will yield higher profits (good for firms) and higher wages (good for employees)
- The adoption of flexicurity-type labor activation policies that include upgrading of skills alongside providing adequate income replacement to ensure financial security for a limited period of time
- Better schools and the encouragement and promotion of lifelong learning and continued on-the-job training, which could benefit both employers and employees

The combination of these improvements will yield higher incomes – that is, win-win for all – in conjunction with the provision of improved coping mechanisms for workers to deal with the hiring flexibility required for greater productivity. The Israeli government's role in this regard requires it to focus on:

- Greater enforcement of existing employment laws and regulations that protect workers while lowering the burden of rigid stipulations that reduce employment flexibility
- Provision of much-improved labor activation policies and income support in times of transition to help employees adapt more quickly to changing economic circumstances while reducing anxiety levels that promote resistance to employer flexibility

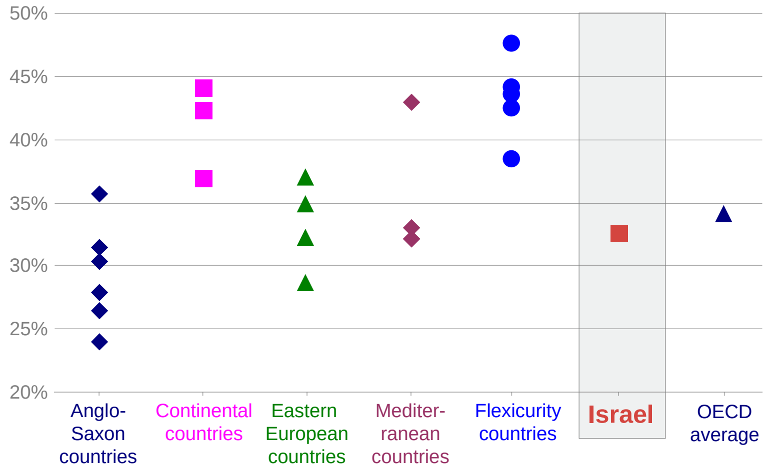
7. Paying for Flexicurity in Israel

Adoption of the flexicurity policies recommended in this chapter will require considerably greater government spending on these issues than in the past. There is a question of where the money will come from. A comparison of tax revenues – or what is commonly referred to as tax burdens – across the various country groupings (Figure 14) shows that the Flexicurity countries are characterized by relatively high levels of taxation, closely followed by the Continental European countries. The fact that the Eastern European countries have considerably lower tax burdens, with yet even lower tax burdens among several Anglo-Saxon countries yields an average OECD tax burden that is only slightly greater than Israel's. However, the figure clearly indicates how low Israel's tax burden is in comparison to the flexicurity countries. In addition, Israel spends much more than all of the other countries (as a share of its GDP) on defense and interest payments on its debt, so it has considerably less left over to finance flexicurity policies under the current state of affairs.

Figure 14

Tax revenue

as percent of GDP, 2011



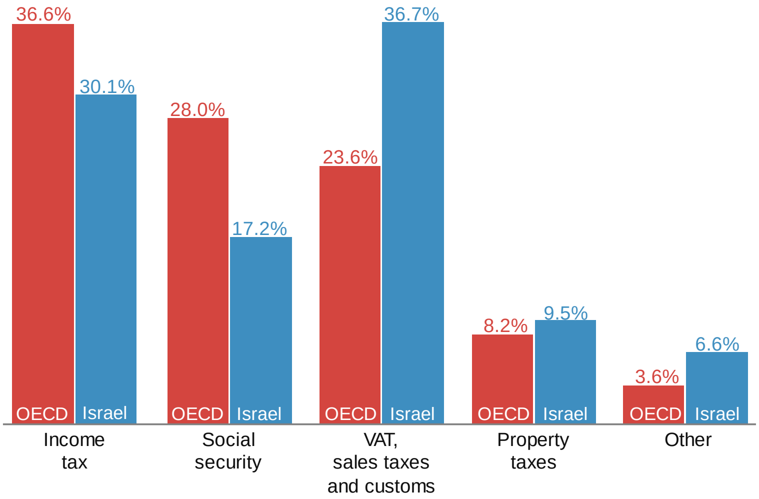
Source: Dan Ben-David and Liora Bowers, Taub Center
Data: OECD

If greater expenditures are needed, where can the resources come from? One option that might emerge from a comparison of Israel and the Flexicurity countries is to simply increase the Israeli tax burden. This then leads to the question: which taxes should be raised? Compared to the OECD, Israel already bases a disproportionate share of its income on indirect taxation, including VAT, sales taxes and customs (Figure 15).[4] Indirect taxes are considered regressive taxes in that they are shouldered more heavily – as a share of income – by the poor than by the wealthy.[5] Thus, a further raising of indirect taxes would place an even greater burden on Israel's poor.

Figure 15

Distribution of total national tax revenues

by tax type, 2011



Source: Ministry of Finance

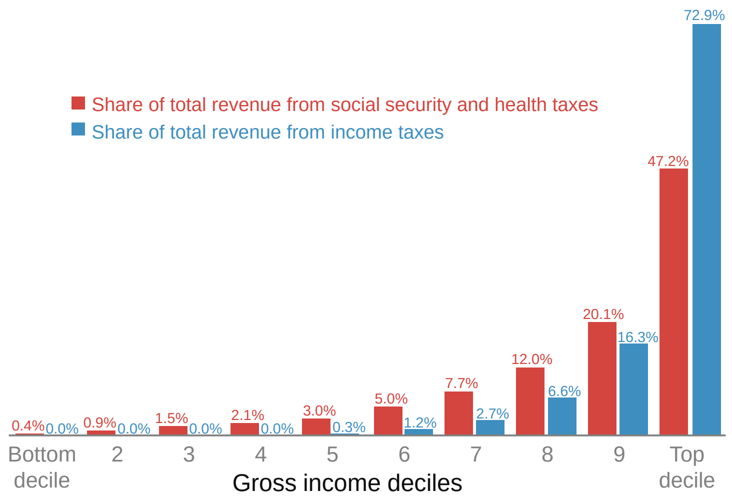
4 The lower revenues from social security taxes in Israel are the result of low contributions from Israeli employers (1.5 percent of GDP in Israel compared to 4.8 percent of GDP in the OECD in 2011). On the other hand, social security taxes paid by Israeli wage earners are 3.8 percent of GDP, compared with 3.1 percent of GDP in the OECD.

5 The poor spend a much greater share of their income on consumption than do

The logical conclusion may then be to increase the government's revenues from direct taxation by increasing income tax rates. However, this route for raising government tax revenues is not quite as obvious as it may initially appear. On the one hand, the share of Israeli government revenues raised from direct taxes is a sixth lower than the OECD average – which would appear to indicate that there is room to raise these. On the other hand, revenues from direct taxation have an extremely skewed distribution in Israel (Figure 16).

Figure 16

Share of total national revenue from direct taxes originating from each income decile, 2011



Source: Dan Ben-David, *A Picture of the Nation 2014*, Taub Center
Data: Ministry of Finance

the wealthy. Consequently, indirect taxes such as VAT comprise a greater share of the poor's income than that of the wealthiest – hence, the term "regressive tax" is applied to them.

A full 90 percent of the country's entire income tax revenue comes from just the top two income deciles, that is, 20 percent of the population contributes 90 percent of the income tax revenues. At the same time, the huge income gaps within Israel are reflected in the fact that a full half of the country does not pay any income tax at all because their incomes are so low that they do not reach the bottom income tax bracket. As a result, there is a serious question about whether it would be possible to further increase the direct tax burden on the few who already shoulder it.

The above two constraints (difficulty in raising the already high indirect taxes any further, and the difficulty in raising income taxes from poor, or increasing the tax burden even further on the very few who actually bear it) are substantial, but not insurmountable. These constraints require a shift in focus from the tax income side to the budget expenditure side. Specifically, a country facing the extreme budget constraints that Israel has to contend with must find the political wherewithal to distribute its limited non-defense budgetary resources with greater efficiency than other developed countries. National priorities need to shift towards budgetary allocations that benefit a greater part of society rather than sectoral, business or personal interests. This is not a pipe dream but an attainable policy option that requires considerably improved budget transparency and substantially improved collection efforts, which in turn require a concerted effort to reduce the shadow economy (Gruber, 2014).

8. Conclusion

Flexicurity emerged as a powerful policy concept in the mid-1990s in Europe, as the debate raged about the effects of job protection on economic growth and social welfare systems. The general requirements for success of flexicurity are flexible labor markets, lifelong learning for employees, active labor market policies and social security systems that provide financial support during transition periods.

Countries with flexicurity are characterized by advantages for employers, such as flexibility in adjustment to competitive demands, access to a skilled work force and low labor relations strife. Advantages for employees include good working conditions, training and upgrading of skills, options for transition and mobility throughout the career cycle, financial security in times of transition and a reduction in labor market segmentation between regular and temporary/fixed-contract workers.

For flexicurity to succeed, both the public and private sectors should be more aligned with regard to employment flexibility. This would require greater flexibility in the public sector, including such practices as: facilitation of hiring from outside the public sector and greater mobility between the public and private sectors; decentralization of human resources management to provide departments and managers with greater discretion; and a closer connection between individual performance and their compensation and promotion. To more closely align with much of the private sector, the public sector (and more inflexible parts of the private sector, such as banking/insurance) also need to move away from the norm of lifelong employment and rigid dismissal and tenure policies.

Substantial budgetary expenditures are required for welfare state and labor activation policies to support and sustain the security aspect of the system. The model places a major emphasis on labor activation to deal more effectively with unemployment. This includes required participation in training or education programs after a short period of unemployment. Likewise, workers are required to accept job offers after a given period of unemployment. Reliance on decentralization is an important facet of the policy, using private sector job training and partnership between the government and employers. In short, flexicurity entails

- a major emphasis on lifelong learning,
- employment contracts that stipulate continued learning,
- career guidance, training and education that is government-supported with employers providing time off,

- and the joint involvement of employers and unions in designing and participating in continued vocational training.

Flexicurity reflects an attempt at finding a win-win arrangement between workers, employers and policy makers. Productivity improvements need to be a fundamental facet of such policies, since these pave the way for higher living standards that enable – among other things – the substantial budgetary costs that accompany their implementation. Therefore, such a solution needs to encompass flexibility in the labor markets, along with financial support for the unemployed (limited in time) and continuous training provided by the government and employers.

Five developed country groupings based on distinct labor and social welfare systems have been identified based on flexicurity indicators (Flexicurity, Anglo-Saxon, Continental European, Eastern European, and Mediterranean countries). The Flexicurity countries are characterized by a relative ease of hiring/firing workers and income and employability security. These countries have generally had very good macroeconomic outcomes and low rates of poverty and inequality. The Anglo-Saxon countries have also been recognized as having good economic results, based on a combination of a highly flexible labor market and lower levels of security. It is important to note that both the Flexicurity and Anglo-Saxon countries experienced larger drops in employment during the Great Recession than the Continental countries that have less flexible labor markets. This put significant budgetary pressure on the already high financial and occupational assistance packages provided to the unemployed in the Flexicurity countries.

Based on flexicurity indicators, Israel falls in a unique position of having higher flexibility than the Flexicurity countries, but even lower levels of security and less investment in active assistance (job placement, training) from the government in case of unemployment than the Anglo-Saxon countries. If Israel wants to move towards greater flexicurity, significant budgetary outlays would have to be made to assist the unemployed, both financially and with training and job placement assistance. Labor activation policies and monitoring systems to counter the disincentives to employment must be put in place.

Labor activation policies should provide incentives to work – both financially through a more substantial negative income tax, targeted at specific populations such as lower-income families, and through stronger enforcement of existing labor protections such as minimum wage and anti-discrimination laws. Investments by the government in infrastructure and transportation, as well as increasing the resources and responsibility of municipalities with regard to local employment will assist Israelis, particularly those in the periphery, in terms of job mobility. Finally, a major opportunity for increased flexibility lies in the public sector, where entry and exit of employees is particularly constrained.

In sectors where unions dominate, employers and unions should collaborate to improve working conditions, benefits and continued education and focus less on job protection. For the benefit of the entire population, there should be much greater commitment by the government and employers to lifelong training. Employers should also encourage internal (adjustable work schedules) and functional (multi-tasking and autonomy) flexibility. Finally, there is a need to reduce labor market segmentation between regular and non-regular (temporary agency or fixed-term contract) workers which often leads to vast differences in protection under the law, as well as the rights and social benefits that each group receives.

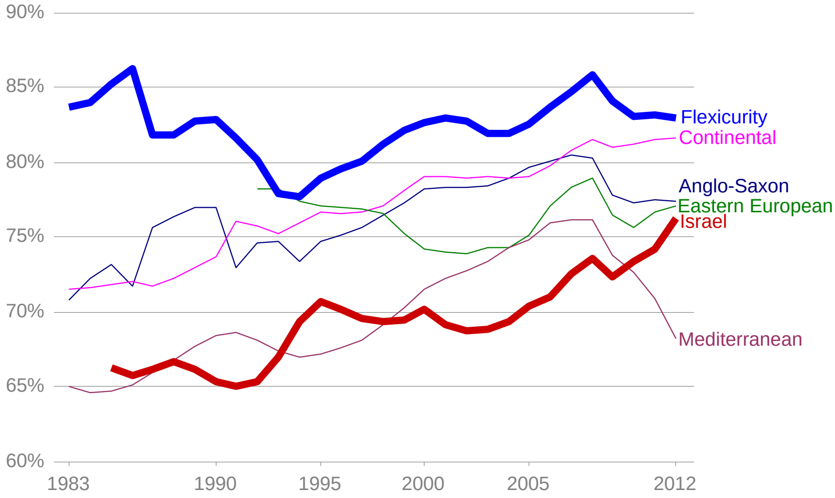
In summary, while implementation of comprehensive flexicurity policy in Israel is not a politically feasible or economically viable option, there are certainly facets of the system that the country can and should implement. The overarching policy goal should be to enhance productivity, growth and employment while providing a serious social safety net that offers Israelis adequate financial peace of mind during transition periods and assistance in improving job skills. These policy options are indeed possible, but their implementation will require an extensive and systemic reassessment of Israel's national priorities.

Appendices

Appendix Figure 1

Employment rates

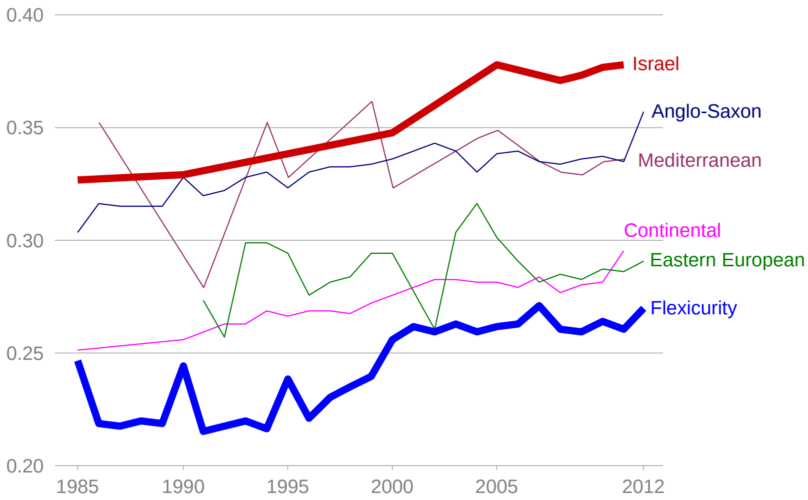
25-54-year-olds, 1983-2012



Appendix Figure 2

Income inequality

Gini Index of disposable incomes, 1985-2012

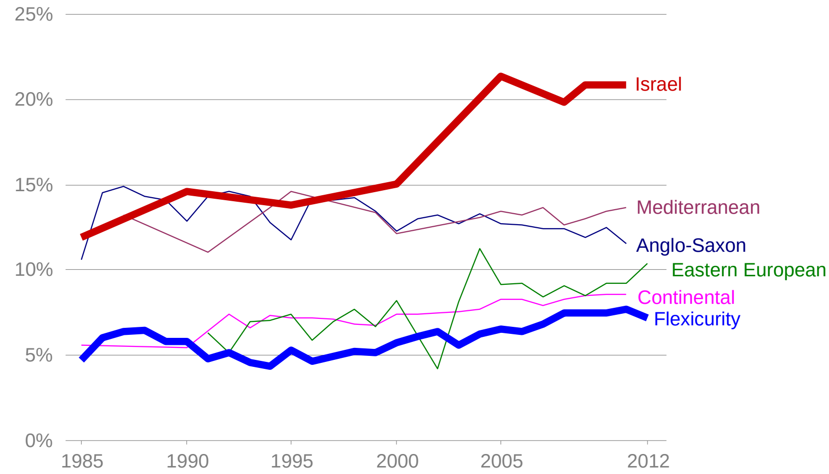


Source for both: Dan Ben-David and Liora Bowers, Taub Center
Data for both: OECD

Appendix Figure 3

Poverty rates

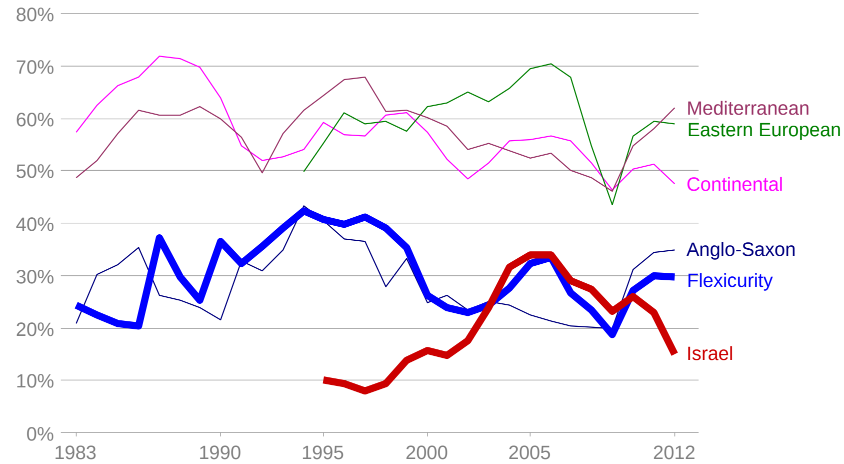
in disposable incomes, 1985-2012



Appendix Figure 4

Percent unemployed 1 year and over

as share of total unemployed, 25-54-year-olds, 1983-2012



Source for both: Dan Ben-David and Liora Bowers, Taub Center
Data for both: OECD

Appendix Table 1. **Flexicurity data on selected indicators in Israel, relative to country groupings**

Index	Anglo-Saxon (1)	Flexi-curity (2)	Conti-nental (3)	Eastern European (4)	Mediter-ranean (5)	OECD	Israel
Flexibility							
Employment Protection Legislation Index (2013)*							
Regular workers	1.55	2.45	2.80	2.29	2.54	2.29	**2.20**
Temporary contracts	0.71	1.88	2.52	2.38	2.78	2.08	**1.58**
Security							
Net income replacement rate for unemployed** (2011)	50%	64%	57%	43%	39%	50%	**41%**
Unemployment benefits/income support (% of GDP, 2011)***	0.54%	1.16%	1.45%	0.45%	1.84%	0.86%	**0.60%**
Active labor market policies (% of GDP, 2011)***	0.24%	1.37%	1.02%	0.32%	0.63%	0.58%	**0.18%**
% of unemployed receiving unemployment benefits (2006-2008)***	49.7%	67.6%	84.3%	30.2%	53.4%	46.1%	**26.6%**
Other measures							
Labor force participation rate (2012)****	79.3%	83.0%	78.7%	77.3%	76.4%	78.4%	**78.7%**
Unemployment rate (2012)****	6.8%	5.1%	5.9%	9.1%	17.2%	7.5%	**5.9%**
Total tax revenue (as % of GDP, 2011)	29.3%	43.3%	41.8%	33.1%	35.1%	34.1%	**32.6%**

(1) Australia, Canada, Ireland, New Zealand, UK, USA; (2) Denmark, Finland, Netherlands, Sweden, Norway; (3) Austria, Belgium, France, Germany; (4) Czech Republic, Estonia, Hungary, Poland, Slovak Republic; (5) Greece, Italy, Portugal, Spain

* The OECD's Employment Protection Legislation Index is on a scale of 0-6 (0 being least restrictive, 6 being most restrictive). The index for regular workers measures how strict regulations are for employers to dismiss workers with open-ended contracts. The index for temporary contracts measures how strict the regulations are on the use of temporary or fixed-term contract workers.

** Net income replacement rate as percent of previous income earned (after taxes and transfers); averaged across various wage rates and family situations; includes social support and other means-tested benefits; average of first 60 months following unemployment.

*** Data not available for select countries.

**** Labor force participation and unemployment rates are for the population aged 25-64.

Data: OECD; International Labor Organization (2011)

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