

# Poor Support for Poor People? Assessing the Impacts of Improving Adequacy in Minimum Income Scheme in Slovakia<sup>1</sup>

Gerbery, Daniel – Miklošovič, Tomáš<sup>2</sup>

Department of Sociology, Faculty of Arts, Comenius University Bratislava

Institute of Economic Research, Slovak Academy of Science, Bratislava

**Poor Support for Poor People? Assessing the Impacts of Improving Adequacy in Minimum Income Scheme in Slovakia.** The paper conceptualizes and quantifies effects of improving adequacy in the minimum income scheme in Slovakia. It builds on previous findings on its significant shortcomings and discusses them in relation to the ideas of activation, active inclusion and social investments. The core of the paper is based on microsimulation of effects of proposed reform scenarios. Three major changes of minimum income scheme's parameters are explored: setting new amounts of minimum income benefit, introducing guaranteed amounts in the minimum income scheme, and change of equivalence scale. The effects are identified in terms of poverty rate, poverty gap, size of target population and budget requirements. Results serve as a basis for discussion on future reforms of the minimum income scheme in Slovakia.

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## Introduction

Periods of positive economic development haven't been used for significant reduction of poverty in the EU. (Collado et al. 2016) Subsequently, the economic and financial crisis has contributed to further deterioration in the living conditions of the most vulnerable populations. The question therefore arises as to how advanced countries should change their welfare state programmes in order to protect people against poverty.

This applies also for Slovakia. Although comparative statistics on income poverty show that proportion of poor population in Slovakia is one of the lowest in the EU<sup>3</sup>, argument often used for strict and sanctioning social policy approach, there is a growing body of empirical evidence that the extent and depth of poverty require more policy effort. The living conditions of poor people relying on minimum income scheme represent the most important example. The minimum income scheme in Slovakia, called *Assistance in material need*, is a social policy programme for households with very low

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<sup>2</sup> Address: Mgr. Daniel Gerbery, PhD., Department of Sociology, Faculty of Arts, Comenius University in Bratislava, Gondova 2, 814 99 Bratislava, Slovak Republic. E-mail: daniel.gerbery@uniba.sk, Mgr. Tomáš Miklošovič, PhD., Institute of Economic Research, Slovak Academy of Science, Šancová 56, 811 05 Bratislava, Slovak Republic. E-mail: tomas.miklosovic@savba.sk

<sup>3</sup> In 2016, at-risk-of-poverty rate represented 12,7 % in Slovakia, compared to 17,3 % in the EU-28 as a whole.

income. It is built upon several components which produce strong conditionality and workfare orientation. Recent studies (Gerbery 2015; Kusá 2014; Lajčáková et al. 2017; Slovenská sieť proti chudobe 2013; Škobla et al. 2016) point to several shortcomings of this programme, including low adequacy, persistence of poverty and deprivation risks, and low integration potential. As persistence and severity of poverty among minimum income beneficiaries have been the most striking problem for a long time, our study aims at exploring and assessing ways of improving adequacy of the minimum income scheme in Slovakia. In this context, we address two general research questions. What are the effects of changing adequacy in the terms of poverty? What are the costs of various scenarios? In order to answer the questions, the microsimulation model EUROMOD, based on the EU SILC data, is used. We develop further previous evaluation exercise (Gerbery – Miklošovič 2016), expanding its scope and methods. Although the study relies heavily on series of technical exercises, they are not self-serving. The purpose is to contribute to discussion on content and meaning of social citizenship and to show potential consequences of specific political choices.

The paper proceeds as follows. In the first part, we present theoretical arguments regarding the role of minimum income programme in advanced societies. Then, the situation in Slovakia is described and main challenges for research are identified. Arguments for selection of the reform scenarios, which become subjects of the assessment, are put on the table too. In the third part attention is paid to the methods of empirical analyses and explanation of methodological and theoretical assumptions. The fourth part brings the assessment of changes in the minimum income scheme. On the one hand, it focuses on changes in headcount poverty rates and poverty gaps (related to the different poverty lines). On the other hand, it pays attention to the costs of the proposed policy reforms. In the final part we discuss the results of the analyses and link them to the debates on poverty reduction in Slovakia.

### **Poverty reduction and role of minimum income scheme**

Poverty can be seen as a lack of sufficient resources for full participation in society. Thinking about poverty in advanced societies means to think about failures of elementary effectiveness of welfare states and their modes of social solidarity. (Ringen 1987) Poverty reduction is not just about one policy measure or one policy initiative, it is matter of broader set of political interventions, including promoting access to labour market, education, health care, housing and building cohesive institutional infrastructure. Both benefits in kind and cash benefits do have redistributions impact. (Cantillon – Vandembroucke 2014)

Despite the fact that progress in reduction of poverty requires complex and coordinated approach, social policy plays a predominate role in this respect. It can address various aspects of socio-economic disadvantages in numerous ways, but the minimum income scheme is of great importance as it provides safety net for the most vulnerable population<sup>4</sup>. The term “minimum income scheme” refers to a non-contributory, means-tested programme for households with very low income which should prevent material destitution and ensure minimum standard of living (Frazer – Marlier 2016: 6), as well as minimize disincentives to paid employment and promote self-sufficiency. (Adema 2006) It represents “the bottom end of welfare state”, the last safety net because it is provided mainly to those who cannot work or access to a decent job and are not eligible for social insurance payments or those whose entitlements have expired. (EMIN 2015) Despite its residual nature, the minimum income scheme is a fundamental pillar of welfare states. Serving as a final form of solidarity, it constitutes foundation of social citizenship rights. (Bahle et al. 2011: 2)

**Table 1: Classification of minimum income schemes in the EU member states**

Category	Countries
Simple and comprehensive schemes	Belgium, Cyprus, Czech Republic, Denmark, Estonia, Finland, Luxembourg, Netherlands, Slovenia, Slovakia, Sweden
Simple and non-categorical schemes with restricted eligibility and coverage	Austria, Croatia, Greece, Hungary, Lithuania, Portugal, Spain,
General schemes with additional categorical benefits which have good coverage	Germany, Latvia, Poland, United Kingdom
Complex network of different, often categorical and sometimes overlapping schemes	France, Ireland, Malta, Romania
Very limited, partial schemes restricted to narrow categories	Bulgaria

Source: Fraser – Marlier (2016: 7). Note: Italy doesn't have a national-wide minimum income scheme; existing programmes at regional or local levels belong to different categories.

Performance of minimum income schemes depends on several factors, among which definition of eligibility conditions, conditionality rules, and relationship with other elements of social protection shouldn't be overlooked<sup>5</sup>.

<sup>4</sup> However, minimum income schemes don't cover all vulnerable groups. There are persons suffering from extreme forms of poverty, deprivation and social exclusion that don't benefit the last safety nets. Non-take up problems, problems with meeting procedural requirements and other factors may contribute to it.

<sup>5</sup> Eligibility conditions mainly relate to residence, household's financial situation, age, and willingness to work. Claimants have to meet various conditions, including registering with public employment services, participating in job search and activation measures, accepting job offers from labour offices, or making use of own assets. As minimum income protection used to cover narrow range of needs, it is often allowed to combine it with other social transfers (child benefits, housing allowances, etc.).

All these aspects are interlinked and their combinations vary widely across advanced societies. Taking into account variety of institutional arrangements, Fraser and Marlier (2016: 7) split the EU member states into five broad categories. (Table 1) On the one hand, there are general, non-categorical schemes, which involve comprehensive schemes (that are, at least formally, open to all people in needs) and non-categorical programmes with more restricted eligibility and coverage exist. On the other hand, there are programmes that use – to the various extent – targeting and thus consist of different schemes for different categories (i.e. lone parents, disabled, working poor). Features of the scheme in Slovakia, which is included among countries with comprehensive schemes, will be discussed later.

The classification shows that there are various ways of how resources are distributed and populations of beneficiaries are defined. But it doesn't reveal probably the most important thing: *what* is granted. It is about adequacy, which is critical for preserving proper functioning of minimum income scheme, i.e. creating conditions for an acceptable living standard that ensures full participation in society. Although idea of defensible standard of adequacy, embedded in the minimum income protection, is one of the pillars of social citizenship, it represents a big problem for welfare states today. Collado et al. (2016: 5) argue that negative trends in poverty in the European countries can be, at least, partly attributed to an increasing inadequacy of minimum incomes. Van Mechelen and Marchal (2013: 21) showed that relationship between minimum income benefit levels and median household incomes/average wages has weakened over recent decades. Decreasing adequacy of minimum income benefits in the majority of the EU countries is confirmed also by the European Commission's analyses (2016: 67).

Eroding capacity of minimum income schemes to tackle extreme forms of poverty and deprivation went hand in hand with increasing focus on work-centred approach and its various forms (work first approach, workfare approach). A linkage between income support and work was reinforced through increasing emphasis on activation and tightening rules for minimum income recipients. Activation paradigms put individuals – their motivation, will, behaviour – at the centre of policy interventions<sup>6</sup>. In addition, shrinking capacities of the EU countries to reduce systematically poverty and social exclusion resulted into efforts to re-frame approaches to poverty at the EU level. The idea of “active inclusion”<sup>7</sup> has brought request for an integrated comprehensive strategy relying on improvements in three areas: adequate

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<sup>6</sup> In this context, concerns about risk of de-politicization of social problems were raised: risk that individualization of causes of social risks could crowd out concerns regarding structural barriers and inequalities and, thus, hamper consolidation of institutional conditions for redistributions. (Serrano-Pascual – Magnusson 2007: 17)

<sup>7</sup> Council Recommendation 2008/867/EEC on the active inclusion of people excluded from the labour market.

income support, inclusive labour markets, and access to quality social services. With regard to adequate income support, the right to sufficient resources was stressed, referring back to the earlier efforts of the European Commission in the field<sup>8</sup>. As the first broader assessment showed (Frazer – Marlier 2013), only limited progress has been made in the implementation of recommended strategies. One of the reasons is ongoing inadequacy of the minimum income protection. Further, the idea of “social investments” came to the fore<sup>9</sup>, with the aim to strengthen people’s current and future capacities to confront social risks. Focus is on long-term investments in human capital development throughout life, enabling policies, including investing in children<sup>10</sup>.

Proposed shift from “old redistributive paradigm” to new enabling, social investments paradigm is not without problems, however. The notion of social investments implies that only some forms of policy interventions produce returns, suggesting that they should be prioritized at the expense of other forms of social spending, which represent – in the situation of lacking returns – a burden. Cantillon made apt comment on this, arguing that “the notion of investments implies a return, and hence one would expect there to be a tendency in social investment policy design first to help forward the relatively strong in the hope that the weaker will be carried along” (2014: 307). She also draws attention to the fact that it is difficult to apply logic of investments in relation to care for elderly persons, disabled, long-term care recipients. In addition, empirical evidence shows that social investments paradigm doesn’t work as expected. (Cantillon 2011)

Recent conceptualizations of anti-poverty policies extend their scope to strengthen preventive measures, activating approach, and economic aspects of social citizenship. Although their contributions are indisputable, the adequate minimum income lies still at the core of any attempts to solve problem of poverty, deprivation and social exclusion.

### **Minimum income scheme in Slovakia: securing living standard of poor people?**

Design of the minimum income scheme in Slovakia, called *Assistance in material need*, continues to be a subject of academic and policy debates. These debates are strongly biased. For a long time, much attention has been paid to disincentives and opportunistic behaviour that the minimum income scheme

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<sup>8</sup> Council Recommendation 91/441/EEC on common criteria concerning sufficient resources and social assistance in social protection systems.

<sup>9</sup> Idea of social investments was formulated well before launching Social Investment Package by the European Commission in 2013. Esping-Andersen and other scholars (2002) contributed to its elaboration.

<sup>10</sup> Broad range policy measures fall within category of social investment policies: education, training, early childhood education and care, activation policies, reconciliation of work and private life policies, etc.

may produce. Adequacy – as core aspect of the programme – has been often left aside. As result, the most minimum income scheme's reforms have focused on tightening rules and increasing conditionality. Today, the minimum income scheme takes the form of poor support for poor people, accompanied by several strict conditions. (For extensive review see Kusá 2014)

However, it was not always the case. In the early 1990s, the social safety net was framed by ideas of fundamental rights. (Kusá – Gerbery 2009: 5) In addition, benefits provided to the minimum income recipients were related to subsistence minimum, an amount which was expected to secure socially acceptable minimum level of income, and were regularly adjusted in line with inflation. Later, several waves of reforms gradually weakened the adequacy-related elements of the minimum income support. The Act no.195/1998 on Social Assistance brought first indices by distinguishing between “objective” and “subjective” reasons for material need what went hand in hand with differentiating the sums of minimum income<sup>11</sup>. Subsequently, as decoupling of the minimum income amounts and subsistence minimum amounts came into play, the subsistence minimum lost its meaning as a real minimum level of living that is guaranteed by society. This situation was confirmed and even reinforced by the wide-range reform in 2003 – 2004 which generated strong workfare-oriented design of the minimum income provision in Slovakia. (Gerbery 2007)

The shift toward residual minimum income provision was framed by ideas borrowed from the global social policy discourse (Kusá 2008) that accompanied the introduction of neo-liberal reforms in the 1980s and 1990s. Ideas of “too generous social security”, “irresponsible behaviour of target group”, “welfare dependency” or “barrier of economic growth and prosperity” were widely used by policy makers, think-tanks and media in relation to the poor and long-term unemployed. Residual and workfare design received support across the political spectrum and it seems to be the only social policy issue on which general consensus was reached, irrespective of ideological roots. The ease, with which the new design of minimum income provision was established and its stability was preserved, resulted also from the ethnic context of the issue. Situation of marginalized Roma communities was often used as a negative example of generous welfare state which induced irresponsible behaviour. (Drál 2008)<sup>12</sup> Development of strict approach to poor people could rely on public attitudes. Although general attitudes toward welfare state and its role show mixed evidence (Strapcová 2005; Džambazovič 2011), poor people (and long-term unemployed) were seen by a significant part of majority as

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<sup>11</sup> Claimants in material need due to so-called subjective reasons were entitled only to 50 % of the subsistence minimum amount.

<sup>12</sup> Paradoxically, these arguments are rehearsed also in the current context, with very strict and low support to poor people.

“undeserving” beneficiaries of social benefits, opposed to old or disable persons.

Recent study on understanding social solidarity (Kusá 2017) reveals that idea of human dignity is not used as an argument for social universalism and, moreover, that support for the universal guarantee of basic living needs is lacking among the public. According to Kusá, this is a consequence of domestic political and societal discourse, which has neglected universalism as a moral value for a long time. This link is supported also by fact that principles of reciprocity and deservingness – which play a prominent role in political discourse – belong to the key arguments people use in relation to social solidarity.

All these features make the adequacy of institutionalised form of social solidarity a fundamental social and political problem. To make a society more inclusive and fairer, the guarantee of basic living standard should become real protection against social risks. Nowadays, three main problems can be identified in relation to low adequacy: low level of minimum income benefit and related allowances, low sensitivity of benefits to number of children in household, and lack of regular adjustment. Low adequacy of minimum income benefits has been confirmed several times by using various indicators. According to Kusá (2014: 26), the difference between the total amount of minimum income package and the amount of subsistence minimum, which is believed to represent a socially acceptable minimum standard of living, is very striking, irrespective of household composition. Moreover, this difference persists even after taking into account the child benefits that are granted to households without means-testing. The gap widens when we compare – for various types of households – the total amount of minimum income package and the at-risk-of poverty threshold, defined as 60 % of median equivalent income.

According to the OECD database on income adequacy, in which the net minimum income levels are expressed as a percentage of median household incomes, adequacy of the Slovak minimum income scheme is low in comparison to majority of the OECD countries. Net minimum income amount for single persons represented 27 % of median household income in 2014. It reached 28 % for couples without children. Families with children are slightly better off: couples with two children (aged 4 and 6) could receive from the minimum income scheme financial resources equal to 29 % of median income in 2014. The same applies to lone parents with two children. Similar conclu-

sions can be drawn by using other databases which compare the minimum net incomes with some general income benchmark<sup>13</sup>.

Low sensitivity to children refers to the fact that the differentiation of the benefit amount doesn't take sufficiently into account number of children in household: families with one child are entitled to the same amount of benefit in material need as those with four children. For families with six or more children the number of children doesn't play the role at all. Moreover, the amounts of benefit in material need have remained unchanged for several years, despite changing prices and general standard of living. The amounts of allowances haven't been changed for even longer period<sup>14</sup>. This status quo is an example of the non-intervention as a reason of decreasing capacity of social transfers to reduce poverty.

Low adequacy, low child-sensitivity and lacking regular adjustment make the minimum income scheme inadequate and dysfunctional. Instead of balancing between two fundamental aims – preventing material destitution and minimizing disincentives to work – it pursues only one of them. But, as the OECD data on inactivity trap<sup>15</sup> show, de-motivation is not universal problem for all minimum income beneficiaries. (Gerbery 2015) There are households, like single parents, for which the safety net creates sufficient financial incentives to move from inactivity/unemployment to employment. In addition, higher disincentives are mainly produced by jobs paid at very low levels (33 % of average wage). Thus, low adequacy does deserve priority attention of public policy and research.

### **How to improve adequacy? Proposed reform scenarios**

The aim of the paper is to evaluate various ways of improving adequacy of the minimum income scheme. While various strategies may be applied, in this paper we can evaluate only some of them. Building on previous work (Gerbery – Miklošovič 2016), we develop and test several new reform scenarios which tackle weaknesses of the scheme. Taking into account the complex structure of benefits and the processes of eligibility assessment and calculation of net amounts, attention is paid to the changes in the “basic” parameters. More specifically, we test the following three kinds of scenarios:

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<sup>13</sup> For example: Comparative Minimum Income Protection Indicators database at the Herman Deleeck Centre for Social Policy (<http://www.centrumvoorsociaalbeleid.be/index.php?q=node/3270>).

<sup>14</sup> In the period 2009 – 2016 following allowances to benefit in material need were provided: protection allowance (EUR 63.07), activation allowance (EUR 63.07), housing allowance (EUR 55.8 for single persons and 89.20 for two or more persons), dependent child allowance (EUR 17.20), special allowance (EUR 126.14 for first six months and 63.07 for next sixth months). Health care allowance was cancelled in 2013.

<sup>15</sup> Inactivity trap refers to an extent of de/motivation to enter labour market (at different wage levels). It measures the part of additional gross wage that is taxed away in the case when inactive person receiving minimum income benefit takes up a job.



1. *Setting new amounts of benefit in material need.* While previous study focused on effects of a gradual increase of existing amounts, here we focus on new proposals, which have a deeper practical and theoretical background. We combine two approaches. Firstly, we employ empirically-driven approach where new amount is defined as average households' expenditure on consumption in the bottom part of the "consumption distribution", using data from the Household Budget Survey 2014 (*Rodinné účty*)<sup>16</sup>. More concretely, we focus on the first 10 % and 15 % households with the lowest consumption expenditure. Secondly, we derive new amounts from existing income standards – minimum wage and poverty threshold – which can be seen as important criterion of adequacy in existing institutional architecture, providing a transparent and meaningful background.
2. *Setting a guaranteed sum of minimum income.* Here we pay attention to the role of the whole minimum income scheme as a guarantor of adequate (although minimal) income. We explore scenarios what would happen if a certain total amount of minimum income were guaranteed. It refers back to the 1990s when the social safety net secured living standard at the level of subsistence minimum. We apply the same approaches as in previous scenario.
3. *Increasing child-sensitivity of benefit in material need through changing its equivalence scale.* Finally, we continue to test new proposals regarding equivalence scale inherent in the minimum income amounts as previous exercise (Gerbery – Miklošovič 2016) showed mixed results. An equivalence scale is used to differentiate amounts of benefits (or legal entitlements) according to the composition of households, defined mainly by number of household members and their age. The differentiation reflects the fact that needs of household grow with each additional member but not in the proportional way (due to so-called economies of scale in consumption). We look at the effects of implementation of two empirically-rooted scales<sup>17</sup>, which are calculated on the basis of real consumption patterns of households with lower level of consumption, as defined above. The scales are derived by comparing expenditure on consumption for single adult, two adults and two adults and child.

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<sup>16</sup> Consumption distribution is defined according to the level of consumption expenditure in following areas: food and beverages, clothing and footwear, housing (water, electricity, gas and other fuels), health, transport, and education. Household Budget Survey is carried out by the Statistical Office of the Slovak Republic and provides information on structure of households' expenditures and incomes.

<sup>17</sup> In previous study (Gerbery – Miklošovič 2016), the widely used OECD scales were tested, including so-called "old OECD scale" which assigns a value of 1 to the first adult household member, of 0,7 to each additional adult and 0,5 to each child.

## Methods and data

Effects of the policy changes are assessed by using EUROMOD, the tax-benefit microsimulation model developed by the Institute for Social and Economic Research at the University of Essex. It contains detailed information on settings and parameters of social security schemes and tax systems in the EU member states and, relying on household micro-data from the EU SILC, it makes possible to calculate the effects of changes in the social benefits and taxes rules on incomes, poverty, inequality, social inclusion and work incentives. (Sutherland et al. 2008: 4) EUROMOD allows to simulate changes in many components of household income, including social contributions, family benefits, minimum income benefits and other. The basic output from EUROMOD is the micro-level change in household disposable income as a result of changes in the parameters of social benefits and taxes. Microsimulation relies on EU SILC dataset from 2012, where all relevant variables (and rules) were updated.

EUROMOD enables us to compute three main policy-relevant estimates. Firstly, we calculate the effects of proposed reforms on the government budget (on a monthly basis) in order to identify various spending levels at which reasonable outcomes can be achieved. Secondly, we estimate impacts in terms of income poverty. Thirdly, we check for the effects on various relevant population categories. When estimating effects on income poverty, we employ three measures. We use especially at-risk-of-poverty rate that is a basic measure of income poverty incidence. It is a standard headcount index, which measures the proportion of population living below the poverty threshold, defined as a 60 % of median equivalised disposable income. In addition, we rely on other poverty-related indicators. We also employ relative median at-risk-of-poverty gap, which expresses the extent to which individuals fall below the poverty line (poverty gap). It is defined as the difference between the median equivalised disposable income of people below the at-risk-of-poverty threshold and the at-risk-of-poverty threshold expressed as a percentage of the threshold. And finally, we use specific indicator called “subsistence minimum gap”. It relates to the specific context of the minimum income scheme in Slovakia and represents a system-specific modification of the “relative median at-risk-of-poverty” indicator. It measures poverty gap among recipients of the minimum income benefit. The “subsistence minimum gap” is defined as the difference between the median income of people receiving benefit in material need and the subsistence minimum. We suppose that this measure is more sensitive to changes in the population of the minimum income benefit recipients, as compared to standard “poverty gap” – relying on general population and “its” poverty threshold – tends to underestimate the effects.

All mentioned indicators are used in the same way: they identify “status quo” before and after the reform proposals are applied to the EU SILC survey sample (the distribution of disposable income). The effects of the proposals are then interpreted in terms of the differences between values “after” and “before”.

### Assessment of effects of changes in minimum income scheme

#### *Setting new amounts of benefit in material need*

Previous simulation-based analysis has shown that very strong increase in the amount of benefit is needed in order to generate significant effects in terms of poverty reduction. At the same time, higher levels of benefit in material need are more effective in reducing poverty gap, as compared to poverty incidence. It has been also shown that the composition of household plays an important role in mediating effects on poverty gap.

Table 2: **Current and proposed new amounts of benefit in material need** (BMN in EUR)

	Currently valid BMN	Proposals referring to households' consumption*		Proposals referring to existing income standards		
		BMN 1	BMN 2	BMN 3	BMN 4	BMN 5
Single adult	61.6	98	115	76	152	174
Couple	107.1	172	195	132	264	302
One parent + one child	117.2	135	160	145	289	331
One parent + two children	117.2	173	204	145	289	331
Couple + one child	160,4	209	240	198	396	453
Couple + two children	160,4	247	285	198	396	453
Couple + three children	160,4	284	329	198	396	453
Couple + four children	160,4	322	374	198	396	453

Notes: BMN 1 = average consumption of the first decile of households with the lowest consumption, BMN 2 = average consumption of the first 15 % of households with the lowest consumption, BMN 3 = 20 % of minimum wage, BMN 4 = 40 % of minimum wage, BMN 5 = 50 % of poverty threshold.

\*The sums of benefit differ also among household types that are treated equally in other scenarios because average consumption was calculated for each household composition.

Here, we take a look at the effects of replacing current benefit's amount by new ones. New amounts of benefit are calculated in two different ways: by referring to real consumption of households and to existing income standards. On the one hand, amounts are calculated as average income for the first 10 % of households with the lowest consumption (labelled as BMN 1) and 15 % (BMN 2), with the aim to capture real expenditures of households at the bottom of the consumption distribution. New amounts cover consumption in the area of food, beverages, clothing and footwear, housing (water, electricity, gas and other fuels), health, transport, and education. Further, new amounts were

calculated as 20 % of minimum wage (BMN 3), 40 % of the minimum wage (BMN 4), and as a 50 % of the at-risk-of-poverty threshold, adjusted for given household composition (BMN 5). Table 2 shows that new ways of calculating benefit lead to higher amounts than existing scheme.

All new proposals have positive effects in terms of income poverty and inequality reduction, although rather of modest magnitude. (Table 3) The stronger poverty-related effects are produced by benefits that are derived from existing income standards. Benefit in material need calculated as 40 % of minimum wage reduces poverty by 9 % (0.01 p.p.) and benefit expressed as 50 % of poverty threshold by 10 % (0.02 p.p.). The extent of poverty reduction is twice as high as in case of consumption-based benefits. The same holds true for reduction of income inequality. The fourth and fifth reform proposals reduce Gini coefficient by 2 %, or 3 % respectively. They also narrow gap between two tails of income distribution (the first and last decile) by 5 and 6 %.

In addition to the modest effects on poverty and inequality, there are strong positive impacts in terms of closing poverty gap. All new proposals, with the exception of benefit calculated as 20 % of minimum wage, contribute significantly to narrowing the difference between the median equivalised disposable income of people below at-risk-of-poverty threshold and the threshold. This is very important fact because it confirms that although not strong in terms of overall poverty reduction, new benefits help the poor people to move towards income standard and, thus, reduce the depth of their poverty. Again, the proposals defined as 40 % of minimum wage and 50 % of poverty threshold have the strongest impact, accompanied by the effect of the benefit calculated as average consumption expenditure of the first 15 % of households with the lowest consumption.

At the same time, however, there are always some costs that must be taking into account in order to make reforms sustainable and politically feasible. Table 3 shows that reduction of poverty and poverty gap requires significant increase in the volume of public expenditure. The higher absolute values of the proposed benefit in material need the higher increase in public expenditure. Calculating benefit in material need as the average expenditure in the first consumption decile would lead to 46 % increase in the public expenditure on the minimum income scheme. Taking into account the first 15 % of the households with the lowest consumption would require 72 % increase in the public expenditure. On the other hand, implementation of the new benefits, defined as 40 % of minimum wage and as 50 % of poverty threshold, would mean that the expenditure will jump even more radically. Put it in another way, each one percent reduction of income poverty induced by new benefit in material need, that is equal to 40 % of minimum wage, is accompanied by 16 % increase in the public resources. In the case of benefit in material need set

at the level of 50 % of poverty threshold, each one percent reduction of poverty requires 19 % increase in the public resources. This is not to say that the strong rise of the costs should hinder the implementation of reforms. On the contrary, any reform related to the minimum income scheme should start with acknowledge that more resources are needed in order to improve coverage of basic living needs of poor population. The question then arises of how a balance between significant poverty reduction and related costs should be defined. Our calculations offer first, although inevitably crude, evidence for this process.

There is also the related issue of changing size of targeted population. An increase in the sums of benefit leads to a rising number of recipients. It is result of the fact that the amount of benefit in material need, which is paid to recipient, is calculated as a difference between the sum of all legally defined entitlements (sum of legally defined benefit and allowances depending on household composition and circumstances) and disposable household income. If the level of benefit in material need will increase, the sum of theoretical entitlements will increase as well. Result is, *ceteris paribus*, extended difference between the sum of entitlements and disposable income. This difference may become so large for some households without entitlement that they can start to claim it. It is worth noting that three scenarios (BMN 2, BMN 4, and BMN 5) produce similar magnitudes of change, but with different results regarding reduction of poverty. So, while setting benefit in material need at the level of 20 % of minimum wage would reduce income poverty by 5 % and lead to increase in the number of recipients by 44 %, using 40 % of minimum wage would improve poverty reduction ability more significantly and the “population effect” would be the same (the same results are produced by benefit in material need defined as 50 % of poverty threshold).

What emerges as an important conclusion here is the fact that due to the existing settings any attempt to improve benefit’s adequacy leads to an expansion of the population of recipients. Two possible strategies may, then, provide food for thought: either this process will be recognized as a necessary part of the scheme and taken into consideration in the preparation of future reforms or it will be challenged as an inappropriate mechanism and new ways of the sums of benefit will be defined. Nonetheless, this issue should attract attention of researchers and analysts when analysing the poverty relief in Slovakia.

Previous analyses confirmed that household composition may serve as an important mediating factor as various household types showed different responsiveness to the changes in the minimum income parameters. In terms of income, situation among households with two, three or four children is markedly improved. Average income of the first 5 % of households with the

lowest income would jump by more than 30 % in the case of scenarios BMN 4 and 5 (income of households with four children would rise by more than 50 %), and by more than 7 % in the case of scenario BMN 3. When consumption-based amounts are taken into account, average income of these households would increase by more than 15 % (BMN 1) or 19 % (BMN 2).

Table 3: **Effects of new amounts of benefit in material need – total population** (percentage change)

	Proposals referring to households' consumption		Proposals referring to existing income standards		
	BMN 1	BMN 2	BMN 3	BMN 4	BMN 5
Percentage change in disposable income of the first 5 % households with the lowest income	+2	+3	+2	+4	+4
Percentage change in at-risk-of-poverty rate	-4	-5	-2	-9	-10
Percentage change in poverty gap	-18	-25	-7	-26	-28
Percentage change in Gini coefficient	-1	-1	0	-2	-3
Percentage change in P10/P90 ratio	-3	-4	-1	-5	-6
Percentage change in expenditures	+46	+72	+19	+145	+185
Percentage change in number of recipients	+34	+44	+22	+45	+45

Source: Authors' calculations, based on EUROMOD

In order to capture effects of our recent proposals, we can also use the indicator called “subsistence minimum gap”. It measures a “distance” between median income of households receiving benefit in material need and relevant subsistence minimum. As such, it is calculated for each main household composition. Microsimulation using the EUROMOD shows that single adults face the strongest improvement of income status in relation to subsistence minimum. As result, median income of recipients becomes significantly higher than relevant subsistence minimum. Similar patterns can be identified for other types of households, although the magnitude of percentage changes in the subsistence minimum gap differ. All in all, applying new sums of benefit in material need would mean that not only distance between median incomes of recipients and relevant subsistence minimum sums disappears, but median incomes exceed the thresholds markedly. Looking at social policy consequences, it would – in average – provide more resources than existing subsistence minimum, which has lost its real content and relevance during the last decades.

#### *Setting new amounts of benefit in material need*

In this part we step further, looking at the effects of re-launching the original function of the minimum income scheme – its commitment to guarantee a

certain income level. We suppose that this level should be related to some normative concept or idea. Therefore, we don't pay attention to the levels determined by empirical approach (i.e. defining amounts on the basis of real consumption of households, etc.). We propose guaranteed amounts (shown in Table 4) by referring to the existing income standards: 50 % of minimum wage and 75 % of at-risk-of-poverty threshold<sup>18</sup>. We choose these two standards because they represent a significant improvement of income situation of recipients and, at the same time, their distance from minimum wage ensures that limited disincentives to take a job are produced.

**Table 4: Proposed new amounts guaranteed by minimum income scheme (in EUR)**

	50 % of minimum wage	75 % of at-risk-of-poverty threshold
Single adult	190	261
One parent with 1 – 4 children	362	496
One parent with 4+ children	528	725
Couple	330	453
Couple with 1-4 children	495	679
Couple with 4+ children	667	915

**Table 5: Effects of guaranteed amounts of minimum income – total population (percentage change)**

	50 % of minimum wage	75 % of at-risk-of-poverty threshold
Percentage change in disposable income of the first 5 % households with the lowest income	+1	+3
Percentage change in at-risk-of-poverty rate	-4	-9
Percentage change in poverty gap	-18	-25
Percentage change in Gini coefficient	0	-2
Percentage change in P10/P90 ratio	-2	-2
Percentage change in expenditures	+22	+146
Percentage change in number of recipients	+13	+32

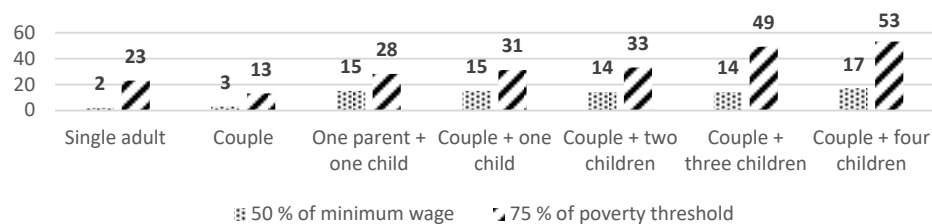
Source: Authors' calculations, based on EUROMOD

If there was a guaranteed amount at the level of 50 % of minimum wage in Slovakia, poverty rate would decrease by 4 percentage points. In addition, depth of poverty would decline markedly – by 18 %. Such step would increase

<sup>18</sup> Originally, we also focused on other scenarios (20 % of minimum wage, 50 % of poverty threshold), but we decided not to elaborate them further because they don't represent an important departure from existing conditions.

expenditure by about one fifth. Number of recipients is expected to grow by 13 %. Applying 75 % of at-risk-of-poverty rate brings stronger effects, reducing poverty by 9 % and poverty gap by 25 %. On the other hand, it is more costly solution, which also induced a more pronounced growth of targeted population. Households with children would benefit the most from both scenarios. They show the strongest growth in average income when looking at 5 % of households with the lowest income. While guaranteeing minimum income at the level of 75 % of poverty threshold, income of couples with four children experience growth by more than 53 % and income of couples with three children by 49 %, compared to rather modest increase for single adult and couples. Using 50 % of minimum wage as a standard maintains the differences, although at lower level. The fact that households with children are winners of proposed reforms is confirmed by changes in the subsistence minimum gap.

**Chart 1: Effects of guaranteed amounts of minimum income – percentage changes in income of 5 % households with the lowest income**



Source: Authors' calculations, based on EUROMOD

### ***Changing equivalence scale***

An ability of equivalence scale to structure appropriately the sums of benefit in material need according to the composition of household is a key feature of the minimum income scheme. The need for reform of the existing equivalence scale, embedded in the sums of benefit in material need, derives from its very low sensitivity to the number of children in household. There are several equivalence scales that can be used for this purpose. They differ by so-called scale elasticity which refers to the power by which benefit amounts (households' needs) change with household size and composition. (Forster – Mira D'Ercole 2012: 33) As we have already mentioned, we focus on implementation of two scales based on consumption patterns of low-consumption households. The two consumption-based scales are defined as follows. "Consumption-based scale 1", based on the consumption of the first 10 % of households with lowest expenditure, assigns a value of 1 to the first



household member, of 0.75 to each additional member and 0.38 to each child. “Consumption-based scale 2”, based on the consumption of the first 15 % of households with lowest expenditure, works with the coefficients 1, 0.7 and 0.39. We suppose that an introduction of new scales affects the number of recipients and level of expenditures, as well as the incidence and depth of income poverty.

Micro-simulated effects on the number of recipients and the volume of expenditure are shown in table 6. In general, changed differentiation of the sums of benefit in material need leads to decline in population of benefit recipients and expenditures level. All reductions are at the expense of childless households and households with smaller number of children. Introducing the consumption-based scale 1 would mean decrease of the number of recipients by 2 %. Expenditures would decline by 3 %. Application of the consumption-based scale 2 would lead to more savings, with the same effect on the number of recipients.

**Table 6: Effects of new equivalence scales on number of recipients and expenditure (percentage change)**

	Consumption-based scale 1		Consumption-based scale 2	
	Number of recipients	Expenditures	Number of recipients	Expenditures
Total population of recipients	-2	-3	-2	-5
Couples	-4	-1	-6	-4
One parents + 1 child	-6	-24	-6	-24
Couples + 1 child	-12	-19	-11	-21
Couples + 2 children	-10	-4	-10	-6
Couples + 3 children	0	+6	0	+5
Couples + 4 children	+68	+37	+68	+35

Source: Authors, based on EUROMOD

It is important to look at effects on different household constellations in more detail because changes in equivalence scale influence directly the distribution of resources among different types of households (by assigning different coefficient to typical members of household). At general level, we can see very similar effects. Both consumption-based scales would lead to a marked increase of the number of recipients among couples with four children. At the same time, they would reduce the number of recipients among all other types of households (with the exception of couples with three children). In relation to the budget requirements – as expected – both scales would re-direct financial resources to households with more children.

The equivalence scales are expected to change income situation in the bottom of income ladder. Table 7 shows the effects on average income in the 1<sup>st</sup> income decile and 5<sup>th</sup> income percentile of income distribution. We can see that households with four children would be the winners. On the other hand, the magnitude of the change is – bearing in mind their very low incomes – rather small. Households with three children benefit from the changes only to a limited extent: slight increase in average income can be found in the fifth percentile. On the other hand, the most significant decrease can be found among one parent families with one child, irrespective of the scale we use.

**Table 7: Effects of new equivalence scales on income in lowest income strata, poverty and poverty gap (percentage change)**

	Consumption-based scale 1				Consumption-based scale 2			
	Income in 5 <sup>th</sup> percentile	Income in 1 <sup>st</sup> decile	At-risk-of-poverty	Poverty gap	Income in 5 <sup>th</sup> percentile	Income in 1 <sup>st</sup> decile	At-risk-of-poverty	Poverty gap
Total population of recipients	-1	0	+1	+4	-1	-1	+1	+5
Couples	0	0	0	+2	0	0	+2	+2
One parents + 1 child	-8	-4	n.a.	+210	-8	-4	n.a.	+208
Couples + 1 child	-3	-1	8	+13	-4	-1	+11	+13
Couples + 2 children	-1	0	0	0	-1	0	0	0
Couples + 3 children	+4	0	0	-9	+3	0	0	-8
Couples + 4 children	+8	+7	0	-80	+8	+7	0	-76

Source: Authors, based on EUROMOD

Note: Microsimulation results for poverty rate among households of one parent with child couldn't be calculated due to data limitations.

What about effects on poverty? At general level, the use of the equivalence scales, accompanied by savings in financial resources, induces a slight deterioration of income conditions, as table 5 shows. At-risk-of-poverty rate would increase approximately by 1 % in general population. Relative median at-risk-of-poverty gap would rise by 4 % or more. There is increase in poverty and poverty gap for couples with one child. Poverty gap for lone parents with one child soars dramatically. It is caused also by low initial value of the indicator. In absolute terms, poverty gap for lone parent would jump to 0.19 (or 19 %, relatively speaking). On other hand, new scales reduce – already low –

poverty gap for households with four children. It seems that efforts to determine equivalence scale by empirical weights, based on real consumption, produce positive effects only in relation to poverty gap and only for households with several children. It doesn't translate into lower poverty rates. Nonetheless, it is an important finding, especially in relation to the previous results referring to the OECD scales. It seems that the changes of equivalence scale don't induce a significant improvement of adequacy. We therefore suppose that more attention should be paid to the level of benefit in material need. In the future, an interaction of changes in amounts of benefit in material need and changes in equivalence scales should be elaborated in more details.

### **Conclusion**

Society that cannot guarantee its citizens a decent, although minimum, living standard is unjust and unfair. Despite the many reforms, the minimum income scheme in Slovakia doesn't work well. Based on disciplining, sanctioning approach it fails to provide protection against extreme poverty and deprivation. The issue of adequacy has been ignored for many years. This fact may reflect general attitudes to poverty and poor people: where blaming approach and de-politicization of social risks dominate, safety programme for poor people remains poor. Social distance and even racial prejudices of general public towards marginalised Roma communities may play an important role too. In this context, it is extremely desirable to re-embed the idea of adequacy in the minimum income scheme and re-start thinking about poverty in terms of social citizenships and social rights.

In our paper we examined ways how to improve adequacy, using the tax-benefit microsimulation model EUROMOD. We presented various scenarios which can serve as borderline cases. Our findings can guide future research and policy debates regarding minimum income scheme reform. As reform of the minimum income scheme is necessary, the only question is, what this step will be like.

Proposals regarding new amounts of benefit in material need and simulated impacts could enrich debates on where the level of more adequate benefit should be set. New amounts have – in general – positive effects on poverty and poverty gap. These positive effects would be offset, however, by radical growth of the number of recipients and expenditures. Taking into account household compositions, average income of the poorest families would increase among households with two, three or four children. These households benefit also from closing the subsistence minimum gap, although the strongest reduction is experienced by single adults.

Aim of the second reform exercise was to draw attention to the role of the minimum income scheme as a guarantor of adequacy. It means that it should

guarantee a certain level of resources which is defined transparently and normatively. We showed that our proposals have positive effects, but their magnitude is not as high as expected, given the increase in expenditure and number of recipients. The question then is – where to draw the line which would indicate minimum, but acceptable level of living, at reasonable costs? Deep and multidimensional poverty makes this reform as difficult as inevitable. But it is clear that without significant volume of additional resources, the problem of poverty cannot be addressed

The final reform proposal focuses on the use of new equivalence scales. It was driven by the fact that existing structure of the sums of benefit in material need is insufficient. Low sensitivity to the number of household members and, especially, to the number of children is striking. Both equivalence scales favour large families, compared to childless couples and households with two or less children. They also help to close the poverty gap for households with several children. On the other hand, these positive trends for specific categories (which suffer most) are partially offset by deterioration of conditions of other types of households. The situation of couples with one child, one parent families and, to certain extent, also childless couples would worsen. At general level, the application of new equivalence scales would lead to increase of income poverty by 1 % and poverty gap by 4 – 5 %, accompanied by marked reduction of expenditures and number of recipients. These results show potential trade-offs for future reforms.

To sum up, we strongly recommend to begin discussion on increasing the sums of benefit in material need. The effects will depend on the pace of increasing and other parameters, but there is evidence that it will help. We also recommend reform of inherent equivalence scale, but its alternation should be selected carefully. It seems to us that use of real consumption of low-income (and low consumption expenditure) households as a basis for calculating weights for household members is not very suitable. And it is very important conclusion for future research and policy debates. The old OECD equivalence scale – that was tested in previous analysis – seems to be better candidate for the starting point. Finally, one general recommendation can be formulated. A simpler design of the minimum income scheme is urgently needed. Existing institutional settings – the legacy of institutional inertia and path-dependency – are too complicated. A complex system of interdependencies hampers efforts to disentangle underlying interactions and processes. Making (future) evaluations more feasible and transparent should be one of the explicit objectives of necessary reconstruction of the minimum income scheme in Slovakia.

*Daniel Gerbery is a research assistant at Department of Sociology, Comenius University in Bratislava and researcher at Institute for Labour and Family Research. His research focuses on sociological analyses of poverty, social*

*inequality, and social policy. He is author of several books and articles in peer-reviewed journals. He serves as a national coordinator of the European Social Policy Network for Slovakia.*

*Tomáš Miklošovič is a research assistant at Institute of Economic Research, SAS, holding a degree from Faculty of Mathematics, Physics and Informatics of Comenius University. His area of academic interest lies in economic modelling of Slovak economy and CGE models. Predominantly he specializes on CGE models, microsimulation and econometric models of Slovakia. He gained practical knowledge while successfully applying models CGE and HERMIN. He co-authored several studies and expert contributions. Besides his research occupation he also maintains a position at Faculty of Pedagogics of Comenius University.*

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