

## Modernising and activating measures relating to work incapacity

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### Background

During the 1970s and 1980s, Sweden was characterised by high and stable economic growth, high and increasing employment rates, and low unemployment rates, fluctuating at 2-3%. However, *short-term* sickness absence was relatively high. Also take up of disability benefits was fairly high and growing, from 5% of the working-age population in the mid 1970s to 7% in 1990.

The severe economic downturn in the early 1990s marked a turning point in Sweden. Unemployment jumped from below 2% in the late 1980s to 8-10% and remained at that level until 1998. Adding those people on sickness and disability benefits, which also increased, more than 20% of the working-age population were receiving social insurance benefits – compared to around 10% during the 1970s and 1980s.<sup>1</sup>

Initially this growth in benefit use was driven by high unemployment rates. However, in the mid-1990s, a new trend was that absence due to *long-term* sickness started to increase and still today one in five in the working-age population draw a social insurance benefit.

Since sickness absence is the main pathway into disability benefits in Sweden, increasing levels of long-term sickness absence transferred into increasing levels of disability beneficiaries. In fact, the annual inflow onto disability benefits more than doubled between 1998 and 2004. As a consequence, the share of the working-age population that lived on either a sickness benefit or a disability benefit peaked at 14% in 2004, the highest level in the OECD.

Historically, there has been a strong negative correlation between sickness absence and unemployment in Sweden. This pattern was clearly interrupted in 2006 when sickness absence started to fall sharply despite a considerable increase in the number of employees. In 2007, a remarkable trend shift occurred when employment rates increased at the same time as both unemployment and sickness absence fell. The falling trend in sickness absence has continued ever since and has had a lowering effect on disability benefit inflow rates. These are now around one-third of the inflow rates in 2004. As a result, also the stock of disability benefit recipients has been affected and is slowly contracting.

The beginning of this major shift in sickness and disability inflow started already in 2004. When the new government took office in 2006, their key priority was to increase labour market inclusion and reduce the number of people relying on health-related benefits. Under the new government, several reforms of the sickness and disability system have taken place. Many of these changes represent a radical departure from previous policies.

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<sup>1</sup> If social assistance payments (provided by municipalities) are included, the share increases to 23%.

## Forward reaching reforms of sickness and disability benefit policies

This section describes some of the policy changes that have taken place in Sweden during the past three years.

Defining a legitimate disability benefit claimant is extremely difficult and in the end a political decision. Such a definition requires in turn a definition of work capacity and a set of tools to measure it. However, having the definition and the tools is not enough because there is also a need to relate the result to some kind of norm. The political decision is then to define this norm. Should this norm be the person's former work capacity or the average work capacity in society or in a specific cohort or perhaps in a specific occupation? Moreover, should this norm refer to the overall or regional labour market situation? If so, should we accept that work requirements would fall in an economic downturn, i.e. that the outcome of the work capacity assessment (or the norm) would fluctuate over time? To answer these questions is almost impossible, which is one reason why outcomes of disability assessments can be arbitrary and unclear. Clearly, most people have a work capacity to some degree, but the probability to find a job differs widely depending on the individual's educational level, occupation and earlier labour market experience. Nevertheless, a well-defined uniform way of assessing work capacity is probably the best way forward, given that a stringent system is in place.

Since the majority of those who take up disability benefits are above the age of 50-55, it is crucial to have an old-age pension scheme that is flexible in terms of when to retire and how to combine work and pensions. But also that entitlements are based on life-time earnings and that entitlements or the pension age are linked to changes in life expectancy.

Past experiences in Sweden has shown that the disability benefit scheme often has been used as an early retirement scheme, sometimes to mitigate increasing unemployment rates, and sometimes to lay off certain people. In short, the disability benefit scheme was used as a labour market adjustment tool. Such a strategy has proven to be very costly both for individuals and society.

A general objective should therefore be to restore the original purpose of the disability benefit scheme by changing the policies that affect negatively employment outcomes. Instead, policies should encourage and help people with a health condition to remain longer in employment or to obtain a better foothold on the labour market.

This requires a comprehensive reform package where several systems are changed. This was very clear from the Swedish unemployment benefits scheme and the sickness benefit scheme, which functioned as communicating vessels. For this and other reasons, Sweden has introduced substantial changes to their old-age pension scheme, tax system and unemployment scheme.

Below is a summary of the most recent reforms the government has launched with the intention to reduce sickness absence, the inflow to disability benefits and the stock of disability benefit recipients. These reforms encompass measures that affect both the supply side and the demand side.

- *To obtain correct and uniform decisions* for all individuals and across the country the Social Insurance Administration went through a comprehensive reorganisation. Note, however, that important work and reorganisations in order to obtain uniform decisions already started in the beginning of the 2000s by the former government and the social insurance authority.
- *To reduce the inflow to long-term sickness*, a new sick-listing process was introduced. Under this new process, the assessment of a person's work capacity is successively widened during the first year on sickness benefits. By the use of clear time frames, the process begins by assessing the possibility to return to the same job and then for a different job with the same employer. It ends with a work capacity assessment towards any job on the labour market.
- *To avoid that people are trapped in long-term sickness*, the maximum time frame on sickness benefits is limited to 2.5 years. Those who at this stage has not regained their work capacity and who are not eligible for a disability benefit are offered an individually adapted labour market programme.
- *To reduce the inflow to disability benefits*, the gateway onto these benefits have been tightened. A disability benefit is nowadays only granted those who have a permanent reduction of their work capacity of such a magnitude that any rehabilitation measure is assumed not to improve their work capacity.
- *To encourage employment among those with a disability benefit*, people who had a disability benefit prior to 1 July 2008 can take up a job or work more without ever running the risk of loosing the eligibility to their benefits. There is a taper rate of 50% for a yearly income of work exceeding € 4 000. People using this option can return to their benefits whenever they like. There are also extensive possibilities for people who were granted a disability benefit after 1 July 2008 to try out work without having their benefit eligibility being re-assessed.
- *To encourage employers to hire people with a reduced work capacity*, employers have the possibility to deduct an amount equal to twice the employer's social security contribution when hiring someone who has been on long-term sick leave or on disability benefits. Moreover, for people on disability benefits, the employer's contribution for sickness benefits has been abolished. Finally, employers do not have to pay sickness benefits for individuals who work and retain their disability benefits.
- *To help people to remain in work or take up a new job*, rehabilitation measures will be better targeted and easier to access by improved forms for financial coordination and local cooperation between the Public Employment Service, the National Insurance Authority, social offices and the health care sector.
- *To encourage job mobility* people has the right to take leave of absence to try out a job with another employer during the first six months on sickness benefits.
- *To support general practitioners* in their sickness certification and to obtain a uniform assessment process, a list has been developed which reports average sickness durations for most diseases, including certain mental health problems.

Currently, the Swedish government is in the midst of improving the system of occupation health service to facilitate earlier identification of health conditions at the work place. The government is also developing new tools to better assess people's work capacity.

Obviously, helping people into employment is a policy that gains everyone. Not only does it help people to avoid social exclusion, it also raises people's incomes, reduces public spending and increases economic output. To be successful requires better incentives for all stakeholders (*e.g.* individuals, employers, social insurance administrations, and the health-care sector) to work, to promote work, to hire and retain people, and to help those persons who can and want to work back to the labour market and into a decent job.