



ESPN Thematic Report on Social Investment Iceland 2015

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EUROPEAN SOCIAL POLICY NETWORK (ESPN)

**ESPN Thematic Report on
Social Investment**

Iceland

2015

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Summary

Iceland shares many of the social investment features of the Scandinavian welfare states, since it is a service-intensive welfare state and has a very high level of employment participation, a very high degree of gender equality, a high level of elderly employment participation, and a high employment participation of disability pensioners, while being more modest on the social compensation side. Iceland also shares some of the characteristics of the societal environments that produce high economic growth rates, flexibility, equality and low poverty levels, compared to the EU countries as a whole.

A highly organized and cooperative labour market, highly geared towards flexibility-security and equality-efficiency compromises, also contributes towards the social investment characteristics of Iceland. Hence there is a fertile ground for win-win complementarities in the Icelandic social policy and labour market environments.

These features however underwent significant strains during the recent crisis, with fiscal consolidation, but seem to have stood the test. While expenditure was cut in some areas, it was also increased in others, including some areas important for social investment goals, such as active labour market policies and rehabilitation.

- Family policy expenditure was increased during the 2000s, particularly on birth leave and day care/pre-school, but the value of the child cash benefit had declined during the decade leading up to the crisis. This benefit was eventually increased by 30% at the beginning of 2013, in a swift reversal of policy.
- Pre-primary and primary educational expenditure was cut by some 13% during the crisis. Subsidies for dental care for children were on the other hand increased significantly. Other parental services and child protection provisions were emphasized by the Welfare Watch, a government organized consultation and advisory forum for surveying welfare setbacks due to the crisis, for early detection of growing problems. These seem to have retained standard reasonably well.

Iceland's very high level of employment participation has been greatly supported by the social investment oriented welfare state and a flexible labour market.

- Child-care (called pre-school in Iceland) is almost universal for children above age 2 and at a very high level for children aged 1-2. The staff-child ratio is one of the best in Europe and the cost of the services is modest, or about 10% of average pay. The municipalities subsidize the operational costs by some 15%.
- Long-term care for the elderly and people with disabilities is at a high level, i.e. comparable to the best in the Nordic countries. This also supports parental employment participation. Both this service and the child-care services were maintained through the crisis close to their pre-crisis standard.
- Maternal/paternal leave schemes however suffered significant cost cuts, which were implemented by placing a cap on the reference pay compensated during the paternal leave. This led to some reduction in take-up rates amongst fathers. This weakening of the birth leave scheme is causing some concern at present.

Unemployment benefit and other aspects of minimum income protection have in general been modest in Iceland compared to the other Nordic nations. The minimum pension guarantee was however raised greatly during the crisis and the unemployment benefit as well as the minimum wage also rose somewhat. These are all above the poverty line for a single pensioner in 2013.

- Iceland uses a flat rate unemployment benefit to a greater extent than the other Nordic nations. That rate is now about 42% of average regular employee pay.
- Active labour market measures were increased greatly during the crisis, to a higher level of participation than found in the other Nordic and EU countries.

This, along with job creation programmes, proved very successful. Unemployment has been halved from its peak in 2009-10. It is well below 5% by end of 2014.

1 Assessment of overall approach to social investment

The Nordic universal welfare states incorporate significant social investment features and have done so for a long time. There is an understanding of social investments as policy and institutional features that improve human capital and facilitate people's participation in economic and social life, thus contributing to efficient economic organization and a thriving society. After all, the Nordic nations pioneered the introduction of active labour market policies during the 1950s and 1960s and became particularly service-intensive in later decades. This thinking was however already evident in the writings of the influential Gunnar and Alva Myrdal during the 1930s in Sweden (Morel, Palier and Palme 2012).

Hence the Scandinavian welfare states have long had a practical component to their social policy, combining social and economic goals as well as economic and gender equality goals that have significantly furthered the social investment approach in later decades.

Iceland shares many of these social investment features since it is a service-intensive welfare state and has a very high level of employment participation (Stefánsson 2012), a very high level of gender equality (WE Forum Gender Gap Report 2013), a high level of elderly employment participation (Special Eurobarometer 378, 2012; OECD 2013), high levels of participation of disability pensioners (Hannesdóttir et.al. 2010), while being more modest on the social compensation side (Ólafsson 1999; Eydal and Ólafsson 2012). Iceland also shares some of the characteristics of the societal environments that produce high economic growth rates, flexibility, equality and low poverty levels. A comprehensive and relatively universal welfare state further contributes to the social investment dimension in Iceland, as well as a highly organized and cooperative labour market, highly geared towards flexibility-security and equality-efficiency compromises (Ólafsdóttir and Ólafsson 2014). Hence there are good grounds for win-win complementarities in the Icelandic social policy environment.

Turning to recent developments of the social investment state in Iceland we can say that Iceland came to the financial crisis of 2008 with a large dose of social investment characteristics. As a part of the crisis responses from 2009 onwards there were however significant expenditure cuts, especially in the areas of welfare services, rather than on cash transfers. Education and health care were significantly hit, as well as public administration and some social services.

Expenditure on labour market activation and rehabilitation were however much increased, greatly championing the investment and (re)activation goals, as we show later in this report (section 2.3.3). Some other aspects of strengthened social investment features can also be mentioned. Thus we would argue that the crisis years since 2010 have seen strains of fiscal consolidation, without however any major destructive consequences to date. Most cuts were met with rationalization, trimming and more efficiency, rather than closure of major service features. As indicated above and further in what follows there were also significant advances in the direction of a social investment oriented welfare state in Iceland during the crisis years and their immediate aftermath.

2 Assessment of specific policy areas and measures / instruments

2.1 Support for early childhood development

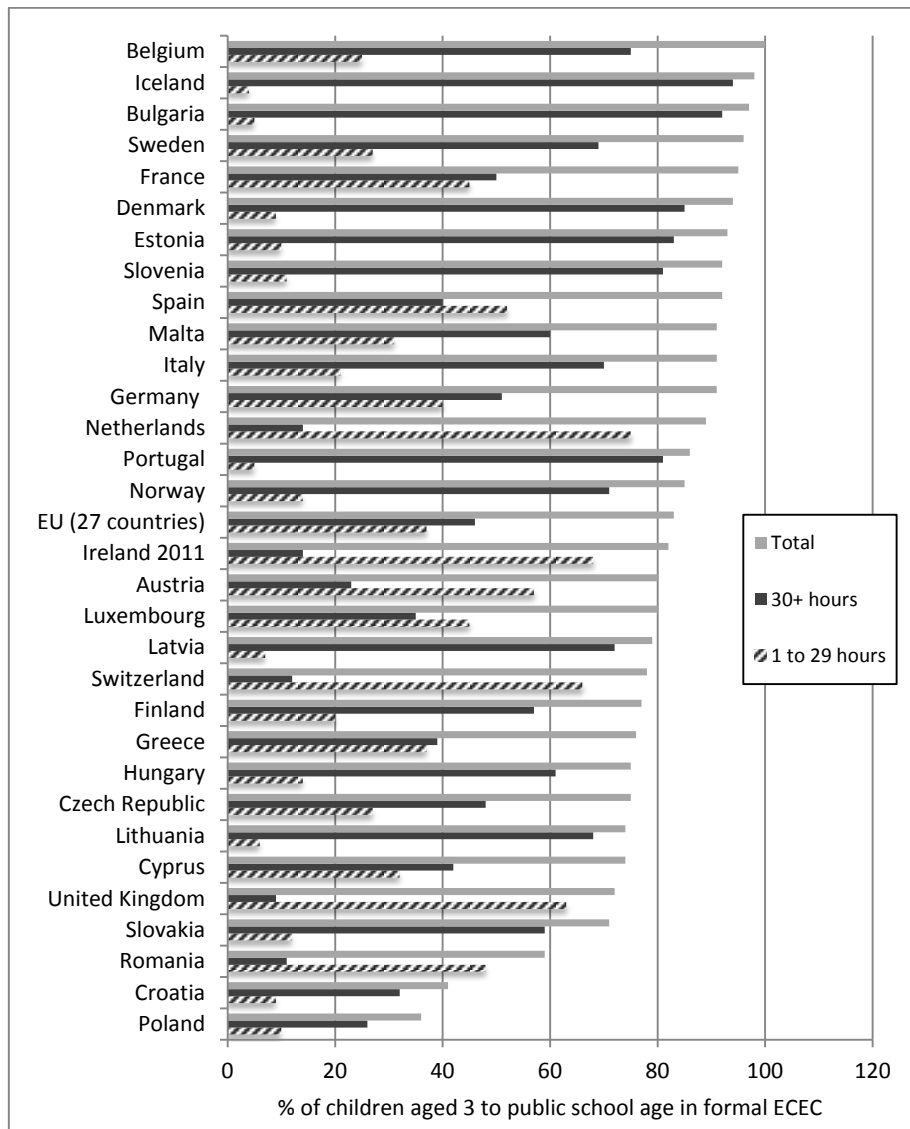
2.1.1 Early childhood education and care

As indicated by Morel, Palier and Palme (2012) the field of family policy has been one of the main avenues of social investment developments in the Nordic nations in recent decades. This has indeed been a decisive aspect of development in Iceland (Eydal 2012). Expenditure on family issues increased significantly during the 2000s, up to the

crisis (Ólafsson 2012). Then it contracted again, reaching bottom in 2012, at a similar level to 2005. In 2013 it increased again. Within the educational budget real expenditure on pre-primary and primary education was increasing up to 2008, when it had a setback of some 13%. This had not yet recovered by 2013. Expenditure on subsidiary services to early education was increasing up to 2010 and then levelled out at a level still higher than prevailed in 2009.

Despite these expenditure developments Iceland remained at a high level in the use of public support for families and children, in a European comparison (Bouget et al. 2015, Annex 3, Table A1).

Figure 1: Early Childhood Education and Care in Europe in 2012: % of children aged 3-public school age in formal child care/pre-school



Source: Eurostat (ESPN Selection of Indicators, prepared by J. Bradbury).

As indicated in Figure 1 Iceland has a very high proportion of children aged 3 to public school age (6) who participate in early childhood education and care (ECEC), in formal day care/pre-school. Iceland comes second only to Belgium in the overall ranking but Iceland has the highest rank of children attending 30 hours or more per week.

The outcome for children under age 3 is also high, particularly for those staying 30 hours or more in formal ECEC (Bouget et al. 2015, Annex 3, Table A3.1).

Subsidies for preschool are also important for parents, enabling them to avail themselves of the high quality pre-school services that are a key element of the social investment approach. The subsidy proportion (i.e. the municipalities' share of the

operating cost) in Iceland was the same as the Nordic average in 2012-13, it was lower in Sweden and higher in Denmark. Iceland has the fourth highest public expenditure on child day care (pre-school) amongst the European countries, indicating also that it is relatively affordable for parents of young children (Bouget et al. 2015, Annex 3, Table A.1).

Iceland has one of the very best child-to-staff ratios in formal day-care/pre-school services (see Statistical appendix: table A4). Hence the quality of the educational and care services provided there should be reasonable.

A major concern after the onset of the crisis was a growing risk of declining dental health amongst children from lower income households. The former government implemented increased subsidies for dental services to those groups and the present government has further developed that provision and extended it to larger age groups. A major step was thus taken in securing the dental health of the younger generation during the otherwise recessive crisis years.

2.1.2 Family benefits

Generous family benefits have been an important characteristic of the Scandinavian welfare approach. Iceland has followed that but at a lower level of generosity for a long time. Iceland's overall expenditure on family benefits (cash and kind together) was the sixth highest in Europe in 2012. In 2008 Iceland was the 4th highest, so the decline during the crisis was not at all drastic (Bouget et al. 2015, Annex 3, Table A2). Looking only at benefits per child however, Iceland had the lowest rate amongst the Nordic countries, with €1,364 while the others spent between €2,265 and €2,561 per child at ages 0-17 (Nososko 2014, p. 66). Still Iceland was at a high level compared to other European countries and the USA.

Iceland is also the only Nordic nation to have the child benefit income-tested to a great extent. That means the cash benefits are targeted significantly at lower income groups and can thus make more of a difference there than indicated by the average figures.

Recent international studies of family cash benefits in Iceland have indicated that the cash benefits to single parents in Iceland are similar to those in the other Nordic nations (Kristjánsson 2010 and 2012). Benefits accruing to couples with children are however in general significantly lower in Iceland, even for relatively low earning couples' households. That is a consequence of the income-testing mechanism biting too hard into receivers' incomes at too low levels. Hence in-work poverty seems to be somewhat higher in Iceland than in the other Nordic countries.

Child cash benefits had been declining in value in Iceland continuously from 1995 to about 2004. Hence Iceland had a better comparative position to the other Nordics in the early 1990s. The benefit was raised after 2004 but did not fully keep up with prices (Ólafsson, Kristjánsson and Stefánsson 2012).

On the 1st of January 2013 the government raised the child benefit by some 30%, responding to studies indicating that families with young children had been amongst those suffering the biggest declines in living standards due to the financial crisis. This was a major step. While that raise has lagged slightly since then, the present government is planning to raise the child benefit again as a compensatory measure to work against higher VAT on food, which took effect at the beginning of this year.

Hence the child benefit regime in Iceland has to a significant extent been revitalized during these times of fiscal consolidation.

2.1.3 Parenting services

Iceland has an extensive system of parenting services, primarily aimed at health care and surveillance, as well as child protection. Nurses visit parents of new babies in their homes and survey the baby's development and guide the parents. No significant changes have been implemented in this area during the last years (Júlíusdóttir 2014).

Iceland had the second highest proportion of children aged 0-17 receiving family support amongst the Nordic nations (preventive counselling, pedagogical support, family therapy, rest-periods etc.; NOSOSKO 2014).

A big concern at the beginning of the crisis was the worry that children might to some extent become victims of their parents' increased difficulties, due to poorer finances and increased unemployment. This issue was particularly monitored by the Welfare Watch, a wide cooperative effort run by ministries and public institutes with NGO's, with the aim of early detection of growing problems.

On the whole Iceland has for a long time had a lower proportion of children under 17 brought up outside the parents' home than in the other Nordic countries and that situation has not worsened during the crisis years (NOSOSKO 2014, p. 64).

On the whole Iceland can be said to possess a relatively strong policy regime for facilitating early childhood development, with a strong social investment characteristic. Iceland's good outcome on UNICEF's 2013 comparison of child well-being is a good indication of that, since Iceland had the third best outcome (UNICEF 2013).

2.2 Supporting parents' labour market participation

Iceland has for decades had one of the highest employment participation rates in Europe. A dynamic labour market has played a role in that, but family policy has also played a large role, not least for facilitating the employment of mothers (both married and single mothers) as well parents with disabilities. Child-care, more commonly called "pre-school" in Iceland, has had the biggest role along with other care provisions and birth leave.

2.2.1 Child care

While Iceland was a laggard in the Nordic community in expanding day-care/pre-school facilities it caught up with the leaders (Denmark and Sweden) between 1995 and 2000 and was in 2013 had about 96% of 3-5 year olds registered in public pre-schools and about 84% of 1-2 year olds (NOSOSKO 2014, p. 58). So the services are now approaching universal level for children above age 2.

In 2012 Iceland had the 4th highest expenditure level for child day care, which had not declined since 2008 (Bouget et al. 2015, Annex 3, Table A1).

As in Denmark, Sweden and Norway, most of the children under age 3 spend 30 hours or more per week in day care, thus strongly supporting mothers' work participation, or in "equality-infused language" it strongly supports double earner teams per household.

For children aged 3 to primary school age about 94% spend 30 hours or more per week in day care/pre-school. That is the highest level in Europe (Bouget et al. 2015, Annex 3, Table A3.2). So the deep crisis of recent years has not affected the standard of child care/pre-school in Iceland in any significant way.

Childcare fees are about 10% of average wages in Iceland in 2012, which is the seventh lowest amongst OECD countries (Bouget et al. 2015, Annex 3, Table B.7).

2.2.2 Long-term care

The development of the long-term care sector in Iceland in recent years has been a success story, unlike the development of health care and hospital services. The governments have actually increased construction of nursing homes during the crisis years. At the same time, the transition from institutional care towards longer stay in own homes for the elderly has succeeded to a great extent. This has been aided by increased home nursing and municipality provided home help services.

Waiting lists for nursing home places became shorter up to 2013, not least because patients were admitted later and their stays were shorter. When individuals are admitted later to the institutions they are in poorer health and have higher service needs. This has in fact been met with a more intense service provision, despite cost

restraints. The pressure on care staff has however increased (ASISP Iceland Report 2013).

On the whole one can say that Iceland has a long-term care service at a very high level compared to EU-countries, and even compared to the other Nordic countries (NOSOSKO 2014, pp. 143-145). This has developed relatively favourable through the crisis and continues to support a very high level of dual employment participation.¹

2.2.3 Maternal/Paternal leave schemes

Iceland had the shortest birth leave provision amongst the Nordic nations in 2013, with 39 weeks of paid leave while the other countries range between 50 and 69 weeks. Since 2000 Iceland has placed a greater emphasis on father's leave of up to 13 weeks. The mother and the father are entitled to 13 weeks birth leave each, after which they can decide which one of them takes the third 13 week period. The father's period cannot be transferred to the mother (NOSOSKO 2014, p. 38).

The compensation level (80%) is also lower in Iceland than in other Nordic countries, since the compensation rate there has a cap close to average pay (370.000 Icelandic Krona in 2014). Iceland still qualifies as a member of the Nordic leave policy regime (cf. <http://www.leavenetwork.org/>). Before the crisis hit the cap was significantly higher but it was lowered repeatedly during the crisis as part of fiscal consolidation. This has lowered take-up rates amongst fathers in the last years. There is now considerable concern about the weakening of the paternal part of the leave programme.

"The Icelandic parliament adopted changes to the law on Parental leave in December 2012, with a staged increase to a 5+5+2 system. Following parliamentary elections in April 2013, a new coalition government came to power. This government deemed state finances to be in such a bad shape that the extension of the leave period adopted in December 2012 could not be carried out. There has been no clear statement on what the future holds; the law has been passed, but continues to await a decision on how it should be financed before it can be implemented" (Eydal and Gíslason 2014).

There is no specific leave provision for taking care of elderly relatives, but working individuals can use their right to sickness absence for that to some extent, but only for a short period.

The main provisions for facilitating parents' labour market participation covered here seem to be relatively advanced in Iceland, in line with the Nordic social investment and social protection regime. This is perhaps best exemplified by the very high rates of employment participation of parents, even during the recent deep crisis years.

2.3 Policy measures to address social and labour market exclusion

2.3.1 Unemployment benefit

Before the crisis, working individuals had a right to unemployment benefit for up to 3 years, with full right to compensation conditional on full 12 months employment during the year prior to the spell of unemployment. When the unemployment problems escalated the right was extended to 4 years. Then in 2013 the new government reduced it again to 3 years and from January 1st 2014 it is reduced further to 2.5 years. This last step has been greatly criticised by the labour union movement.

Those who fully use their right to unemployment benefit due to long-term unemployment have to rely on Social Assistance from the municipalities. The sum

¹ In Bouget et al. 2015, Annex 3, Table B2, it is indicated that Iceland's expenditures on long-term care have collapsed from 1.75% of GDP in 2006 to 0.3% in 2007 and 2008. This is completely unfounded. OECD figures for this in the year of 2011 are 1.7% of GDP (cf. OECD 2013a, p. 187) and have more or less remained at that level through the crisis.

available from that source is lower than the unemployment benefit. The Ministry of Welfare announced in early January 2015 that it will be proposing new legislation to allow conditioning the receipt of Social Assistance with active job search by those applicants able to work. That is in line with the Ministry’s emphasis on returning as many as possible to the labour market. Hence the activation emphasis is strengthened.

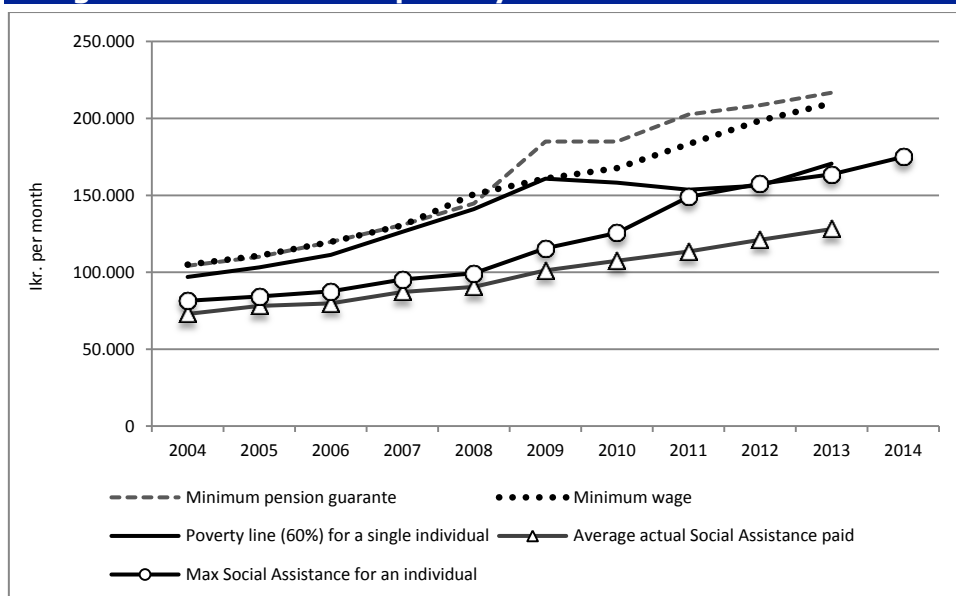
The unemployment benefit is 70% of previous pay for up to the first 3 months and after that individuals get a fixed sum per month, with some supplement for children in their care. The flat rate benefit is now 184,000 IKr per month (about €1,210), or about 42% of average regular employee salary. It has traditionally been at the lower end compared to the other Nordic countries (Kristjánsson 2010; NOSOSKO 2014, chapter 4). The unemployment benefit was raised a little during the depth of the crisis while average wages remained unchanged (and lagged greatly behind prices).

Expenditure on unemployment benefits went from one of the lower in Europe in 2008 to about the EU average by 2010. It has come down significantly again from 2012 to the present, with a rapid contraction of unemployment in those last years (Bouget et al. 2015, Annex 3, Table C1). The unemployment rate in Iceland is now well below 5% (i.e. by the end of 2014).

2.3.2 Minimum income

Minimum income for working individuals is the bargained minimum wage, for pensioners it is the minimum pension guarantee, the flat rate unemployment benefit for the unemployed and for those falling through these security nets it is the Social Assistance. Iceland has a high minimum pension guarantee, a modest unemployment benefit, a modest minimum wage and rather low Social Assistance allowance. Figure 1 shows the level and development of the minimum wage, the minimum pension and the Social Assistance allowance in relation to the 60% poverty line for a single individual, from 2004 to 2014.

Figure 2: Minimum wage, minimum pension guarantee, average social assistance paid per individual, maximum social assistance per individual living alone and the 60% poverty line 2004-2014



Sources: TR (2013) and Statistics Iceland

The minimum wage and pension guarantee were at a similar level from 2004 to 2008, higher than the poverty line. Then with the crisis policies these benefits and guarantees to the lowest income groups were specifically raised for sheltering these groups. We see in the figure how that went through the crisis, with these sums galloping well ahead of the poverty line. In 2013 the unemployment benefit was lower, but still somewhat above the poverty line. Hence poverty rates were contained during

the depth of the crisis. Expenditure on Social Assistance in Iceland was about 50% above the EU average in 2012 (Bouget et al. 2015, Annex 3, Table C2).

The maximum Social Assistance allowance for an individual living alone was significantly below the poverty line from 2004 to 2010, but from 2011 it was more or less in line with the poverty line. Municipalities have long been criticised for keeping the Social Assistance allowance low and in fact below the poverty line, but that changed during the crisis, as figure 1 shows. Hence everyone should be secured an allowance at least close to the poverty line or above, from 2011 and onwards. The average actual Social Assistance allowance paid per individual is however considerably lower than the maximum right, reflecting the fact that many Social Assistance seekers have some other means of subsistence, which reduces the SA Allowance actually paid, due to means-testing. The maximum SA allowance should therefore be the societal minimum that everyone should be entitled to – and that is not far from the poverty line.

These facts are an important explanation of the low poverty level that prevails in Iceland, both before and after the crisis (Bouget et al. 2015, Annex 3, Tables C10, C13, C14, C15a, C15b, C15c, C15e).

UNICEF's 2014 report on child poverty features a poverty rate for 2013 anchored in the real poverty line of 2008. This produces a big increase in child poverty in Iceland (second only to Greece). This reflects the big fall in median real earnings from the elevated height at the top of the bubble years (when the Icelandic Krona was significantly overvalued). Still, the poverty rates (both relative and material deprivation) in Iceland remain low in 2012 and 2013, even though financial hardship of households has indeed worsened, due to the overall lowering of real earnings power.

2.3.3 Active labour market policies

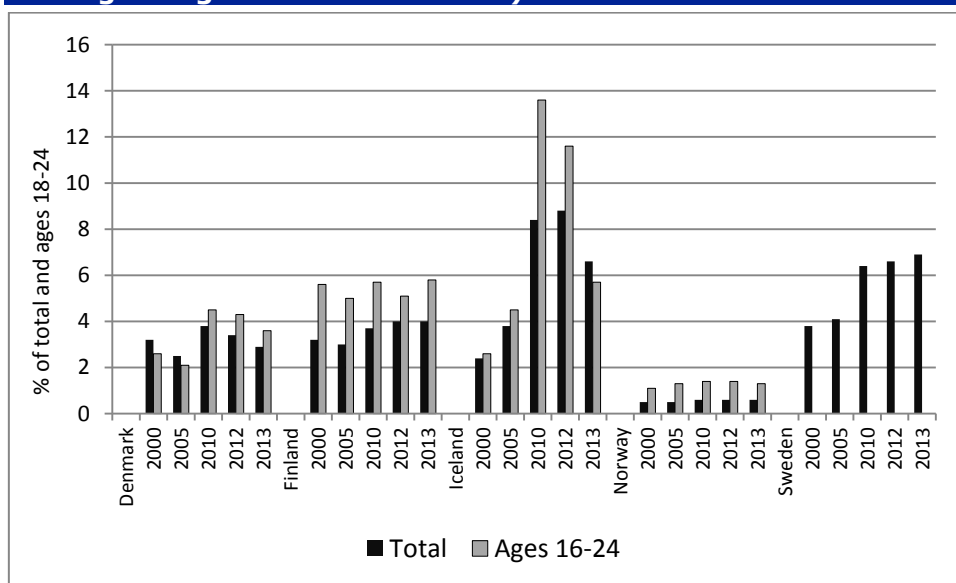
When the crisis hit in autumn of 2008, Iceland's unemployment rate went from less than 2% to above 8% in 2009. Even though this was not particularly high by international standards it was the highest that Iceland had experienced during the whole of the post-war period. This caused great concern and the government responded both with increasing job creation efforts and greatly increased targeted activation and rehabilitation programmes to counter the trend.

So even though active labour market policies (ALMPs) have for long been a part of the Nordic welfare regime they were not advanced in Iceland due to the lesser need, given Iceland's long-term very high employment participation rates and low unemployment. Expenditure on active labour market measures (job search, education, employment subsidies, training etc.) were however increased by some 60% from 2008 to 2010 and participation in programmes soared (Ólafsson 2014; Maskína 2014). Figure 2 shows this development in a Nordic comparative context.

By 2010 Iceland had greatly surpassed the participation rates in active labour market measures that had prevailed in the other Nordic countries. The concentration on youth unemployment is well reflected in the columns for 18-24 year olds.

The rather swift reduction of unemployment from 2011 onwards, down to one of the lowest unemployment rates in Europe in 2014, is a telling story of the flexibility of the Icelandic welfare policy environment. The shift from greatly increased numbers of unemployment benefit receivers to greatly increased activation and rehabilitation efforts reflects the strength of the practical side of Iceland's social policies.

Figure 3: Active labour market programmes' participation, 2000-2013: Intra-Nordic comparison. All unemployed individuals and those aged 16-24 (data lacking for ages 16-24 in Sweden)



Source: Nososko 2014

We believe that the joint emphasis on job creation, participation in activation programmes, participation in educational and skill enhancing programmes, as well as temporarily subsidised job offers (wage subsidies for 6 months from the unemployment benefits fund) contributed to the evident success of the overall efforts at reducing unemployment since 2011.

2.3.4 Social services

The directorate of Labour (Vinnumalastofnun - <http://www.vinnumalastofnun.is/>) provides assistance with job search, including through its own Public Employment Services – PES). But it also provides counselling, short training courses and it facilitates re-entry to formal education, for example at secondary level and above. These services were greatly increased during the crisis, as shown above. The labour market partners run organized short-term courses for life-long training (FRÆ-Fræðslumiðstöð atvinnulífsins - <http://www.frae.is/>). That did not change greatly during the crisis.

All employed individuals have access to the services of the Directorate of Labour and to the labour market educational facilities (FRÆ). In addition those who suffer accidents or illness and lose their employment have since 2008 had access to the new services of the Labour Market Partners' Rehabilitation Services (VIRK - www.virk.is). There are however hardly any one-stop shops for overall access to Public Employment Services and other social services or social protection benefits. The Ministry of Welfare is however presently seeking to increase the possibilities for providing more one-stop-shop services for public social security and labour market services.

The Social Assistance allowance in the Reykjavik commune is partly conditional on receivers taking part in a job search programme (if capable of working) or taking part in a personal plan for increasing their workability. In that sense the social services in Reykjavik and other larger municipalities contribute to increased activation and a better efficiency of the active labour market policies. If SA receivers refuse to take part in such work-oriented programmes their SA benefit can be cut in half for the month that they reject such an offer and also for the following month. Hence there is a punitive clause in the rules for SA benefits (see rules here: http://eldri.reykjavik.is/desktopdefault.aspx/tabid-4547/7777_read-31627/).

On the whole we can say that the Icelandic social investment and the social protection environments work well together and also with the labour market and the economy in general, producing valuable synergies. This environment aids in the achievement of the joint goals of equality and efficiency, justice and growth, participation and flexibility. That seems to be well in line with the highest goals of the EU's social investment strategy.

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