

Flexible Labor in an Inflexible Environment

Reforms of Labor Market Institutions in Bosnia and
Herzegovina in a Comparative Perspective



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1.

Introduction

The labor market in Bosnia and Herzegovina (BiH) faces serious problems: in 2014, the employment rate was at a very low 31.7%, and the unemployment rate for persons 15 and above was as high as 27.5%.¹ Wartime destruction of industrial infrastructure, loss of business networks due to the dissolution of Yugoslavia, inadequate adaptation to the new business and technological environment, as well as unsuccessful privatization processes in the post-war transition period are some of the factors that have negatively impacted both the creation of new and the maintenance of existing jobs. The consequences of this state of affairs include a low labor force participation and high structural unemployment, migration of the working age cohort to other countries, the unresolved status of workers “lost in transition,” as well as social insecurity and a high poverty rate.

Although there is consensus in BiH that the *status quo* is unsustainable, labor market reforms to date have been slow and partial, lacking a clear vision of the labor market model to be pursued. Recently, labor market reforms have found their way onto the agenda of decision-makers, primarily due to the obligations BiH undertook towards the International Monetary Fund (IMF) within the *stand-by* arrangement, as well as commitments under the “Reform Agenda,”² which is “closely aligned with the aims of the EU’s new approach to economic governance in the Western Balkans.”³ The Agenda has been adopted by entity and state-level governments in the context of acquiring candidate status for membership in the European Union (EU). Reform proposals in this area have also been articulated within the “Compact for Growth and Jobs” (CGJ) initiative of the European Delegation to BiH, as well as the BiH Council of Ministers’ *National Economic Reform Programme* (NERP) for BiH for 2015. To encourage employment and creation of new jobs, reform proposals primarily focus on increasing the flexibility

¹ Unemployment and employment rates according to the definition of the International Labor Organisation (ILO). BiH Agency for Statistics, *Anketa o radnoj snazi, 2014: Konačni rezultati* [2014 Labor Force Survey: Final Results] (Sarajevo: BiH Agency for Statistics, 2014), pp. 31, 37.

² The Reform Agenda contains a series of measures in various areas, including the labor market, and is supported by: the European Union, the International Monetary Fund, the World Bank, the European Bank for Reconstruction and Development and a host of governments and international institutions “Reform Agenda for Bosnia and Herzegovina 2015–2018,” Working translation, final version, p. 1.

³ Ibid.

of working conditions by improving the labor law and changing collective agreements⁴, but also by reducing the tax burden on labor.⁵

The proposed reforms are primarily concerned with increasing labor market flexibility, but to a lesser extent pertain to issues of protecting workers and their income security in the event of unemployment, and are only marginally concerned with the issue of employability (e.g. through lifelong learning, active employment measures, etc.), even though these are important aspects of the “flexicurity” policy in the European Union. In other words, the current discourse on policy change in the field largely disregards important elements of the labor market. This begs the question to what extent reform proposals have taken into account the existing institutional environment of the BiH labor market and how the flexibility of working conditions, as the key aspect of reforms, would affect labor market performance in interaction with the institutional environment.

Concerning the above, this study rests on the assumption that different reform options should be considered in their wider institutional context. This would mean focusing not only on the impact of labor legislation on labor market performance, but also on the impact that institutions, such as collective bargaining mechanisms, policies, programs and the institutional framework for employment, social insurance policies, minimum wage, labor taxation and making work pay policies, as well as existing configurations of institutions, have on labor market performance. Based on insights into policies and practices in the labor market realm in other European countries, particularly the European Union, this study aims to contribute to an understanding of available reform needs and options, and their possible implications for BiH.

In order to assess the state of the labor market and the reform path in BiH, the analysis is situated within a wider conceptual framework that defines the basic terminology, indicates important elements of the labor market and provides an overview of the main discussions and their implications for public policies in this field. A more detailed analysis is performed with respect to employment protection legislation, labor cost and taxation, collective bargaining mechanisms, and employment policies.⁶ Comparative experiences from other European countries are taken into account in order to consider possible reform paths, but

⁴ “Reform Agenda for BiH,” pp. 4-5. See International Monetary Fund (IMF), *Bosnia and Herzegovina: Sixth and Seventh Reviews Under the Stand-By Arrangement and Requests for Augmentation of Access and Modification of Performance Criteria* (IMF: 2014), p. 15. See also: EU Delegation to BiH, *Compact for Growth and Jobs in BiH* (Sarajevo: EU Delegation to BiH, 2014), p. 6; International Monetary Fund (IMF), *BiH: Letter of Intent* (IMF: 2014), p. 10.

⁵ For example, reducing the contribution rate for health insurance is proposed in the medium-term period, which would entail comprehensive reform of the healthcare system. IMF, *BiH: Letter of Intent*, p. 7. See also: EU Delegation to BiH, *Compact for Growth and Jobs in BiH*, p. 5; Council of Ministers BiH, *National Economic Reform Programme for 2015* (Sarajevo: Council of Ministers of BiH, 2015), pp. 107 and 120.

⁶ The study does not consider professional development and training and lifelong learning systems in more detail, given that they fall outside the scope of labor market institutions.

also to understand the impact of different institutional and other contextual factors on labor market performance⁷. European countries are used as points of comparison, not just because of their similar institutional environments and the European perspective of BiH, but also because current reform proposals heavily rely on EU standards and practices in this domain.

In terms of methodology, this is a comparative study that combines multiple methods of data gathering: a review of secondary literature and available statistical indicators, an analysis of the institutional and legal framework in BiH and EU countries, and semi-structured interviews with representatives of organizations and institutions in BiH involved in different aspects of the BiH labor market or in labor market reforms.⁸ Given that this research is limited by the dearth of important statistical indicators about the BiH labor market, and also given the fact that it was conducted for the purposes of a study that aims to inform an expert debate in the context of public policy making in this domain in BiH, it is important to note that it does not aim to explain the impact of various contextual factors on the performance of the labor market in BiH. Such analyses would certainly be useful for a better understanding of the BiH labor market, but they fall outside the scope of this study.

An overview of conceptual debates in the domain of the labor market and its institutions is given below. This is followed by an overview of BiH labor market dynamics and trends, various BiH labor market institutions in comparative perspective, and concluding remarks.

⁷ Gøsta Esping-Andersen and Marino Regini, "Introduction," *Why Deregulate Labour Markets?* eds. Gøsta Esping-Andersen and Marino Regini (New York: Oxford University Press, 2000), p. 2.

⁸ These are nine interviews with representatives of different organizations and institutions, including representatives of entity governments, employment institutes, unions, employers' associations, international organizations and the academic community.

2.

Debates on the Labor Market and Its Institutions

Viewed in the context of current international debates in the realm of the labor market, current BiH labor market reform proposals seem to considerably neglect a number of important aspects. In the first place, their primary focus is on the possible positive outcomes of increased flexibility of working conditions, such as the creation of new jobs; however, they do not reflect upon the potential negative impacts of flexibilization of working conditions that are often brought up in discussions in this realm, such as reducing the security of workers and job quality. Within the current discourse on reforms, “European standards” are often invoked as the frame of reference for what the BiH labor market is supposed to achieve, while neglecting the fact that there are great differences between EU countries in terms of the organization and functioning of their labor markets, which are certainly influenced by differences between the economic models of these countries. Finally, even though international literature indicates the importance of interactions between different labor market institutions, which can also affect the outcomes of reforms on one or more institutions, it seems that the reforms are not being evaluated within the broader institutional environment of the labor market.

Therefore, this chapter first gives an overview of key debates concerning flexibilization of working conditions, followed by a discussion of the typologies of varieties of capitalism and welfare states and their relation to labor market institutions. Finally, the debates about the interaction between labor market institutions, as presented in the relevant literature, are discussed.

2.1. For and Against Labor Market Deregulation and Flexibilization

In the past few decades, the most prominent debate in the labor market realm concerns labor market deregulation and flexibilization of working conditions. While some believe that flexibilization would lead to the creation of new jobs and enhancement of economic growth, others claim that it will not effect fundamental change, but will decrease long-term investment in workers,

undermine social consensus or cause conflict due to social inequality.⁹ This debate has been on-going since the economic crisis in the 1970s when states started abandoning Keynesian macroeconomic policies. Such policies had, based on the assumption that insufficient demand and market fluctuation were the cause of high unemployment and low growth, sought to maintain stability by intervening in the economy by way of monetary and fiscal policy. It was believed that the Keynesian concept could not explain the simultaneous rise in inflation and unemployment during the crisis,¹⁰ and state policies and recommendations of international financial organizations¹¹ came to be dominated by the neoliberal economic paradigm based on “budgetary rigour, wage restraint, monetarism and corporate competitiveness.”¹²

In the new paradigm, a “rigid” labor market was identified as the main cause of high unemployment and low growth. This discourse was particularly supported by the influential OECD Jobs Study (1994), which is seen to have blamed the rigidity of the institutional environment and the lack of flexibility of working conditions and wages for slower growth and high unemployment in European economies.¹³ Social benefits, previously used as a countercyclical measure during recession, were considered a cost and the cause of low motivation among the unemployed to find jobs.¹⁴ The OECD recommended deregulating working conditions in order to adapt to market pressures, reducing employment security and reforming unemployment benefit systems, as well as the shift from passive to active labor market policies.¹⁵ As noted by Morel et al, “unemployment was thus interpreted as a microeconomic problem of market distortions linked to strong job protection, high minimum wages and generous unemployment insurance, rather than as a macroeconomic problem of insufficient demand.”¹⁶ At the same time, flexibility of working conditions was believed to be necessary due to the reorganization

⁹ Esping-Andersen and Regini, “Introduction,” p. 1. See also Sandrine Cazes and Alena Nesporova, “Introduction,” *Flexicurity: A Relevant Approach in Central and Eastern Europe*, eds. Sandrine Cazes and Alena Nesporova (Geneva: ILO, 2007), p. 1.

¹⁰ Nathalie Morel, Bruno Palier and Joakim Palme, “Beyond the welfare state as we knew it?” In *Towards a Social Investment Welfare State? Ideas, Policies and Challenges*, eds. Nathalie Morel, Bruno Palier and Joakim Palme (Bristol: The Policy Press, 2012), p. 5, p. 7.

¹¹ For further detail, see Richard B. Freeman, “Labour market institutions without blinders: The debate over flexibility and labour market performance,” *International Economic Journal* 19, no. 2 (2005), pp. 129–132.

¹² Morel, Palier and Palme, “Beyond the welfare state as we knew it?” p. 7. See also Freeman, “Labour market institutions without blinders,” p. 129.

¹³ See Organisation for Economic Co-operation and Development (OECD), *OECD Jobs Study: Evidence and Explanations* (Paris: OECD, 1994).

¹⁴ Morel, Palier and Palme, “Beyond the welfare state as we knew it?” p. 7.

¹⁵ Richard B. Freeman, “Labor market institutions around the world,” Working paper series (Cambridge: National Bureau of Economic Research (NBER), 2007), p. 3. See also Freeman, “Labour market institutions without blinders,” p. 131.

¹⁶ Morel, Palier and Palme, “Beyond the welfare state as we knew it?” p. 7.

of industrial production in response to increased international competition and rapid technological innovation, which was not always compatible with centralized and uniform rules determining modes of production and working conditions.¹⁷

Deregulation entails changing the regulatory framework to make firing and hiring of workers easier, or to enable adjustment of wages and working hours. It can also pertain to replacing laws or tripartite arrangements with decentralized collective bargaining.¹⁸ Flexibility, on the other hand, refers to the ability of adjustment to market conditions, as follows¹⁹:

- 1) **External numerical or employment flexibility:** Entails the adjustment of the number of workers and the use of “flexible” contracts (fixed-term, part-time, etc.).
- 2) **Internal functional or technical-organizational flexibility:** Pertains to adjusting terms of reference or employment positions within a company, and usually includes retraining and development of new skills. It promotes horizontal and vertical mobility within the company.
- 3) **Wage or financial flexibility:** Pertains to adjusting the level and the structure of wages.
- 4) **Flexibility of working time/temporal or internal numerical flexibility:** Pertains to adjusting the number of working hours (working in shifts or part-time, overtime, etc.).

The type of flexibility will depend on the labor market’s institutional environment, social norms, as well as a company’s organizational and marketing strategies. For example, companies whose production is based on quality usually depend on functional flexibility due to the importance of developing new skills and innovation. For mass production, which rapidly adapts to changes in demand, external or wage flexibility is of greater importance.²⁰ There is a trade-off between these modes of adjustment, given that numerical flexibility may diminish the readiness of workers to accept organizational changes and attend training, while companies will find it harder to reduce wages or lay off workers in the event of organizational adaptation.²¹

Arguments in favor of increasing the flexibility of working conditions start from the assumption that labor market institutions may influence an increase in unemployment and a decrease in employment. However, research conducted to

¹⁷ Marino Regini, “The Dilemmas of Labour Market Regulation,” in *Why Deregulate Labor Markets?* eds. Gøsta Esping-Andersen and Marino Regini (New York: Oxford University Press, 2000), p. 13; Manuela Samek Lodovici, “The Dynamics of Labour Market Reform in European Countries,” in *Why Deregulate Labor Markets?* eds. Gøsta Esping-Andersen and Marino Regini (New York: Oxford University Press, 2000), p. 32.

¹⁸ Regini, “The Dilemmas of Labour Market Regulation,” p. 24.

¹⁹ *Ibid.*, pp. 16, 17, and 26.

²⁰ *Ibid.*, p. 17.

²¹ *Ibid.*, p. 21.

date using statistical analysis of the impact of various labor market institutions on aggregate employment and unemployment and other indicators of labor market performance in various countries has not produced clear, unequivocal results to confirm such assumptions. Authors of recent research studies, as well as organizations such as the OECD, claim that there is little to no evidence of impact of institutions on employment and unemployment.²² On the other hand, some analyses have shown that employment protection legislation can slow down labor market flows,²³ meaning that it will take more time for the unemployed, especially those belonging to categories that are not easily employable, to find jobs,²⁴ and that labor market institutions influence the structure of unemployment in that way.²⁵ Furthermore, there is strong evidence that mechanisms of collective bargaining – as an important labor market institution – can lead to a decrease in pay inequality,²⁶ and encourage long-term investment in workers through education and training.²⁷

Despite the contradictory findings on the effects of flexibilization of working conditions, during the 1980s and 1990s, numerous European countries applied strategies of partial flexibilization,²⁸ meaning that fixed-term and part-time contracts were made more flexible, as were seasonal and other atypical employment contracts. Even though such employment arrangements made it easier for many groups with hindered access to the labor market, such as youth, women, low-skilled and long-term unemployed persons, to find jobs, this led to a segmentation between those employed permanently (*insiders*) and unprotected workers (*outsiders*). In this constellation of relations, “employees with atypical contracts carry the burden of adjustment to economic shocks.”²⁹ Empirical research has shown that labor market dualization, i.e. the creation of a gap between protected (usually high-skilled) and unprotected (usually low-skilled) workers, is particularly common in the service industry, and that wage adjustment is one of the key tools for creating jobs for the low-skilled workforce

²² For a detailed overview of research in this area, see Organisation for Economic Co-operation and Development (OECD), *Employment Outlook 2013* (Paris: OECD, 2013). See also Sabina Avdagic and Paola Salardi, “Tenuous link: labour market institutions and unemployment in advanced and new market economies,” *Socio-Economic Review*, No. 11 (2013), p. 745. According to Freeman, findings of very influential studies from the 1990s were later refuted for, among other things, not using robust statistical models. Freeman, “Labor market institutions around the world,” pp. 20–21.

²³ OECD, *Employment Outlook 2013*, pp. 71–72.

²⁴ Gøsta Esping-Andersen and Marino Regini, “Conclusions,” in *Why Deregulate Labour Markets?* eds. Gøsta Esping-Andersen and Marino Regini (New York: Oxford University Press, 2000), p. 337.

²⁵ See Regini, “The Dilemmas of Labour Market Regulation.”

²⁶ Freeman, “Labor market institutions without blinders,” p. 137.

²⁷ Avdagic and Salardi, “Tenuous link,” p. 745; Regini, “The Dilemmas of Labour Market Regulation,” p. 26.

²⁸ *Ibid.*, p. 2.

²⁹ Elke Viebrock and Jochen Clasen, “Flexicurity and welfare reform: a review,” *Socio-Economic Review*, No. 7 (2009), p. 311.

in this sector.³⁰ In underdeveloped economies in particular, dualization pertains to a gap between formal and informal employment, that is, undocumented, untaxed employment that is not subject to employment protection legislation.³¹ The consequences are inequality and discrimination (e.g. on the basis of gender, age, ethnicity), as well as reduced production efficiency,³² given that temporary workers mostly face a higher degree of uncertainty and that employers invest less in them, which decreases the professional development and productivity of such workers.³³

2.2. Towards Flexicurity: A Declarative or Substantial Labor Market Policy?

Due to the increasingly prominent problem of a dual labor market, as well as increased unemployment and slow growth in many European states, public policy in this realm is also slowly shifting. It is believed that in order to be truly successful, labor market policies should have an integrated approach,³⁴ such as policies of *secure flexibility* or *flexicurity*, which combine the flexibility of working conditions with measures to provide security.

Flexicurity is proposed as a welcome compromise between flexibility and security in the labor market³⁵. Although it is presumed that a more dynamic labor market will help workers find jobs corresponding to their skills and facilitate career advancement and pay increase, research has shown that increasing flexibility of employment terms may increase the number of lay-offs.³⁶ Laid-off workers suffer losses in terms of income, accumulated skills and experience, and in the case of long-term unemployment, also deterioration of health.³⁷ According to the OECD, the potential repercussions of deregulation would have to be offset by adequate unemployment benefits and programs to enhance workers' employability.³⁸ The small open economies of Denmark and the Netherlands,

³⁰ Regini, "The Dilemmas of Labour Market Regulation," pp. 19–20.

³¹ Simon Deakin, *Addressing labour market segmentation: The role of labour law* (Geneva: ILO, 2013), p. 1.

³² Ibid. See also Viebrock and Clasen, "Flexicurity and welfare reform," p. 311.

³³ Organisation for Economic Co-operation and Development (OECD), *Employment Outlook 2014* (Paris: OECD, 2014), pp. 17–18.

³⁴ Deakin, *Addressing labour market segmentation*, pp. 1–3.

³⁵ Ruud Muffels and Ton Wilthagen, "Flexicurity: A new paradigm for the analysis of labor markets and policies challenging the trade-off between flexibility and security," *Sociology Compass* 7, no. 2 (2013), p. 111.

³⁶ OECD, *Employment Outlook 2013*, p. 107.

³⁷ Ibid, p. 68.

³⁸ Ibid, pp. 66–68.

which have achieved significant recovery of their labor markets during the 1990s,³⁹ are considered successful examples of applying flexicurity policies.

The concept of flexicurity combines different dimensions of flexibility and security (Table 2.1), and this is usually a certain level of flexibility of working conditions and security of employment and income. Employment security is achieved through investment in worker employability, e.g. through active employment measures or lifelong learning programs,⁴⁰ and income security through unemployment benefits.⁴¹

Table 2.1. Flexibility and Security Dimensions

Flexibility Dimensions	Security Dimensions
<i>External numerical:</i> Adjusting the number of workers	<i>Job security:</i> Certainty of keeping a job
<i>Internal numerical:</i> Adjusting working hours	<i>Combination security:</i> Certainty of having a work-life balance
<i>Wage:</i> Adjusting wages	<i>Income security:</i> Certainty of receiving an adequate and stable level of income in the event of unemployment
<i>Functional:</i> Internal reorganization of workers	<i>Employment security:</i> Certainty of keeping paid work, e.g. through education and training

Source: Adapted from Wilthagen and Tros (2003, 2004)⁴²

Flexicurity is an important component of European Union policy in the labor market realm, as set out in the *Guidelines for the employment policies of the Member States* (2010), the *European Employment Strategy*, the *Europe 2020 Strategy* and many other documents.⁴³ According to some sources, the approach advocated by the European Commission is closest to the type of flexicurity applied in Denmark, that is, a combination of relatively low employment protection with generous social security schemes, active employment policies

³⁹ Viebrock and Clasen, "Flexicurity and welfare reform," p. 306; Muffels and Wilthagen, "Flexicurity: A new paradigm," pp. 112 and 114.

⁴⁰ Muffels and Wilthagen, "Flexicurity: A new paradigm," pp. 112–113.

⁴¹ Ibid, p. 114.

⁴² In Viebrock and Clasen, "Flexicurity and welfare reform," pp. 308–309.

⁴³ See, for example: European Commission, Green Paper, Modernising labour law to meet the challenges of the 21st century, COM (2006) 708, (Brussels: European Commission, 2006); European Expert Group on Flexicurity, Flexicurity Pathways Turning hurdles into stepping stones (Brussels: European Commission, 2007); European Commission, Towards Common Principles of Flexicurity: More and better jobs through flexibility and security, COM (2007) 359 (Brussels: European Commission, 2007); Council of the European Union, Towards Common Principles of Flexicurity – Council Conclusions, SOC 523, ECOFIN 503 (Brussels: Council of the European Union, 2007); European Commission, An Agenda for new skills and jobs: A European contribution towards full employment, COM (2010) 682 (Strasbourg: European Commission, 2010); European Commission, Employment Package (Brussels: European Commission, 2012), "Council Decision of 21 October 2010 on guidelines for the employment policies of the Member States," *Official Journal of the European Union* 2010/707/EU.

and lifelong learning programs.⁴⁴ Although EU member states are obliged to report on their progress in applying flexicurity principles, the European Commission recognizes that, due to the specificity of institutional environments and diverse challenges in the labor market, member states cannot have identical approaches.⁴⁵ As the main challenges faced by different member states in the labor market, the European Expert Group on Flexicurity identified a segmented labor market, lack of transition between jobs, limited access to education and training for marginalized groups and persistent long-term unemployment and informal employment.⁴⁶ The recommendation is to address these challenges through flexible and reliable employment protection legislation, comprehensive lifelong learning strategies, effective active labor market policies and modern social security systems.⁴⁷

Other organizations have also adopted the flexicurity concept to a greater or lesser degree. For example, this concept is used in the Global Employment Agenda of the International Labor Organization. Some authors believe this concept has also influenced the discourse of the OECD so that this organization increasingly stresses the importance of social policies and employment protection in the context of the labor market.⁴⁸ The latest job quality indicators of the OECD focus on labor market security, quality of the working environment and the level and distribution of earnings, while taking into account numerous important aspects of the institutional environment of the labor market (e.g. employment protection legislation, the system of compensation in the event of unemployment, active employment measures, social dialogue and collective bargaining mechanisms, access to quality education and training, etc.).⁴⁹ While EU-level employers' associations support this concept, the European Trade Union Confederation was initially skeptical due to fears of an increase in atypical forms of employment and expansion of the secondary, non-unionized labor market, and has questioned wage flexibility and increased discretionary powers of the management in determining wages based on performance. In the meantime, the Confederation has supported the flexicurity model as applied in the Nordic countries and Austria as a way to improve growth in Europe. The degree of acceptance of this concept varies among EU member states, and in many of them unions are not fully supportive of flexicurity.⁵⁰

⁴⁴ Viebrock and Clasen, "Flexicurity and welfare reform," p. 322.

⁴⁵ Muffels and Wilthagen, "Flexicurity: A new paradigm," p. 116.

⁴⁶ Ibid.

⁴⁷ European Expert Group on Flexicurity (2007), in Viebrock and Clasen, "Flexicurity and welfare reform," p. 311.

⁴⁸ Viebrock and Clasen, "Flexicurity and welfare reform," pp. 322–323.

⁴⁹ OECD, *Employment Outlook 2014*, pp. 17–18.

⁵⁰ Viebrock and Clasen, "Flexicurity and welfare reform," pp. 323–324.

Namely, flexicurity has been criticized on a number of grounds. Some believe that, given its multi-dimensionality and different configurations in practice, the concept is too vague.⁵¹ It is also said that many policies are lumped in under flexicurity, even though they potentially aim to increase only flexibility or only security.⁵² Critics also believe that the EU is only declaratively advocating flexicurity principles without providing for their detailed operationalization or application. There are also dilemmas about the extent to which the EU is truly promoting both sides of flexicurity. Some claim that this concept has merely replaced the previous discourse on activating the unemployed without introducing anything new.⁵³ It is also believed that in promoting flexicurity, the European Commission prioritizes economic over social goals.⁵⁴ Auer doubts the possibility of reaching a consensus on the concept in view of growing criticism from unions, at the national and EU level, who see it as “flexibility in disguise,” owing in part to the perception of its unbalanced application.⁵⁵

Although discretion in choosing the modality of flexicurity is justified by differences in labor market performance,⁵⁶ some believe that it may undermine the meaning of the concept. A 2013 European Commission study on the state of flexicurity in the EU showed that flexicurity policies have not been widely applied in member states, largely due to the financial crisis, and that labor market flexibility in many of the member states has increased over the past ten years. Meanwhile, increased flexibility has not been accompanied by an increase in security; instead, security has even decreased.⁵⁷

Precisely because differences in the institutional environment and economic situation of various countries heavily influence approaches to flexicurity, the possibility of applying the Danish or Dutch model is questionable. Some authors believe that positive labor market performance in Denmark and the Netherlands cannot be attributed solely to flexicurity policies, but are also accounted for by other important elements, such as macroeconomic conditions, wage policies and collective bargaining mechanisms.⁵⁸ Although the European Commission report claims that the effects of the economic crisis were milder in countries where

⁵¹ Ibid, p. 325.

⁵² Ibid, p. 310.

⁵³ Ibid, p. 325.

⁵⁴ Maarten Keune and Maria Jepsen, “Not balanced and hardly new: The European Commission’s quest for flexicurity,” Working Paper (European Trade Union Institute for Research (ETUI), Education and Health and Safety, 2007), pp. 12–13.

⁵⁵ Auer (2010), in Viebrock and Clasen, “Flexicurity and welfare reform,” p. 326.

⁵⁶ Muffels and Wilthagen, “Flexicurity: A new paradigm,” p. 115.

⁵⁷ European Commission, *Flexicurity in Europe* (Brussels: European Commission, 2013), p. 34.

⁵⁸ Keune and Jepsen, “Not balanced and hardly new,” p. 6. See also Viebrock and Clasen, “Flexicurity and welfare reform,” p. 326.

flexicurity policies were being applied, it also states that numerous historical and institutional factors also influenced the economic situation in such countries.⁵⁹

2.3. Understanding Institutional Differences between Countries

As demonstrated through the above discussions of labor market flexibility and security, there is consensus around the fact that Europe is not a homogeneous whole as far as the labor market is concerned. In other words, there is no more talk of “sclerotic Europe” or the “European experience,” as opposed to experiences of other countries such as the USA. Although they do not follow and cannot account for institutional changes within countries, the typologies of *varieties of capitalism*⁶⁰ and the *welfare state*⁶¹ from the realm of political economy and social policy are often used to explain the differences between institutional environments of companies and social protection systems of countries, thus providing a frame of reference for discussions of possible reform options applicable in a given context.

Literature on varieties of capitalism makes the basic distinction between *coordinated market economies*, such as Germany, Finland and the Netherlands, and *liberal market economies*, such as the UK, Ireland and the USA. As their name suggests, coordination between unions and employers forms the basis of coordinated market economies. Apart from determining wage policies, social partners play a key role in developing education and training systems based on specific professional qualifications and skills as integral parts of production strategies. In Germany, for example, sectoral employers’ associations and unions define categories of skills and training protocols to be subsidized by the state, in line with the needs of their sector. In this type of economy, employers’ associations encourage companies to take on apprentices and monitor their participation in apprenticeship schemes. Workers are thus provided with guarantees for their efforts, and thanks to uniform wages in the sector, companies are protected from competitors luring away their employees. Generally speaking, employers’ associations are informed about the situation within companies, and are also responsible for monitoring the development of their corporate governance systems. On the other hand, unions coordinate with workers’ councils at company level in order to provide protection to workers from arbitrary lay-offs and derogation of working conditions. Another feature of these economies are

⁵⁹ European Commission, *Flexicurity in Europe*, pp. 3–4.

⁶⁰ Peter A. Hall and David Soskice, eds, *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage* (New York: Oxford University Press, 2001).

⁶¹ Gøsta Esping-Andersen, *The Three Worlds of Welfare Capitalism* (Princeton: Princeton University Press, 1990).

financial systems that provide companies with long-term access to finances (e.g. through local banks) so that they may retain their workers through times of crisis and invest in long-term projects.

When it comes to liberal market economies such as the UK, the central role in determining relations within the economy is left to market forces. The conditions under which companies acquire access to financing depend considerably on their performance in the capital market, and investors (shareholders) estimate the value of the company based on publicly available information. This financing model means that companies must take into account current revenues and share prices and adjust the number of workers, their wages, etc., accordingly. Given that employment is determined by the market, the management has discretionary powers to lay off workers, companies are not under the obligation to form representative workers' bodies, and unions are, generally speaking, weak. Given that the system is not based on investment in long-term production strategies and skills specific for a company or sector, individuals invest in general skills that can be acquired through secondary and higher education.⁶²

This typology later came to include the *mixed market economy* of South European countries (e.g. Greece, Italy, Portugal, Spain, and some countries of Eastern Europe). In this variant of a coordinated economy, the state plays a central role by compensating for the lack of independent self-organization of workers and companies. Social partners do not have the capacity to generate collective goods such as training systems, innovations, social security for workers or wage adjustment, as is the case in the coordinated model. They make use of privileged access to the state to maintain their privileged positions, and often use connections with political parties to lobby the state. In the event of a crisis, the competitiveness of a sector is not protected through wage adjustment mechanisms, but instead, due to a drop in competitiveness, economic operators use their "traditional reservoir of political influence to maintain standards of living."⁶³

The conclusion that the social security of workers depends to a large degree on the capacity for agreement among key interest groups is also found in literature dealing with welfare states, which provides a complementary categorization of European states based on their level of social protection. It thus comes to distinguish between the *continental/corporatist, conservative* model (e.g. Germany) primarily based on social insurance for the active population, the *liberal model* (e.g. the UK and Ireland) where social benefits are limited to the

⁶² Peter A. Hall and David Soskice, "Introduction," in *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*, eds. Peter A. Hall and David Soskice (New York: Oxford University Press, 2001).

⁶³ Anke Hassel, "Adjustments in the Eurozone: Varieties of Capitalism and the Crisis in Southern Europe," Discussion Paper Series (London School of Economics, 2014), pp. 8-10; Also see, Bob Hancke, Martin Rhodes and Mark Thatcher, "Introduction," in *Beyond Varieties of Capitalism: Conflict, Contradictions, Complementarities in the European Economy*, eds. Bob Hancke, Martin Rhodes and Mark Thatcher (New York: Oxford University Press, 2007).

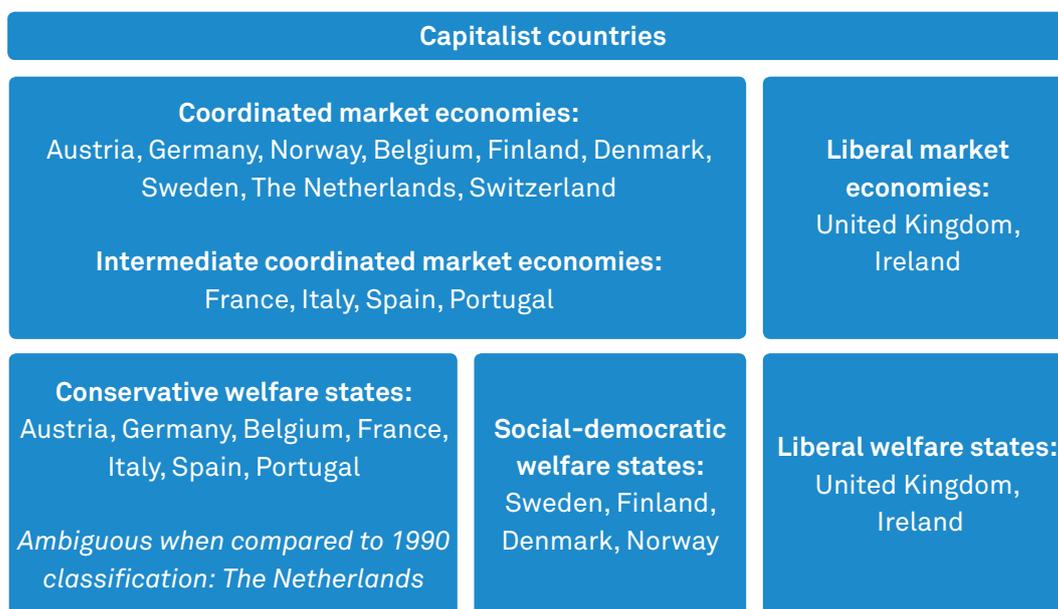
poorest categories of the population, the universal *social democratic* model of protection (e.g. Scandinavian countries), and the *southern* model (a variation of the continental model) traditionally providing a low level of social protection to all parts of the population apart from the employed.⁶⁴

In the context of the labor market, the *continental/corporatist (conservative)* regime is dominated by employment protection legislation, institutional negotiation on working conditions, and relatively low unemployment benefits. Social security is primarily based on social insurance schemes and depends on employment status, which means that income support during unemployment is mostly guaranteed to a protected group of full-time workers. Coverage by collective agreements is usually much greater than the rate of unionization due to the obligation to apply collective agreements in each sector.⁶⁵ On the other hand, in the *liberal* model, employment protection legislation is mostly limited to cases of violation of workers' rights, such as unfair dismissal. Industrial relations are decentralized and uncoordinated, while decisions on the level and structure of wages are made at the company level. The *social democratic* model guarantees citizens the right to comprehensive and generous protection from risk through various benefits and social services, and has highly developed active employment policies and other services for the unemployed. Determining wages and regulating working conditions is a matter of centralized agreement between unions and employers. In the *southern* continental regime, full-time employees are protected, while external flexibility is ensured through short-term and atypical contracts, early retirement schemes financed by the state, and partially through widespread self-employment and small businesses that are not subject to labor regulations. Graph 2.1 gives an overview of the classification of European states based on these typologies.

⁶⁴ See, in general, Esping-Andersen, *The Three Worlds of Welfare Capitalism*; and Francis G. Castles et al, eds, *The Oxford Handbook of the Welfare State* (New York: Oxford University Press, 2010).

⁶⁵ Lodovici, "The Dynamics of Labour Market Reform in European Countries," pp. 33–35.

Graph 2.1. Select European states classified according to welfare state regimes and varieties of capitalism



Source: Adapted from Schröder, 2013.⁶⁶

In other words, the nature of the economy and the type of system of social protection are important factors that will inevitably affect labor market institutions, such as employment protection legislation, employment policies and social security of workers, and need to be taken into account when considering possible labor market reforms and their outcomes.

2.4. Interactions between Institutions

The conceptual debates and experiences in applying various labor market reform policies to date have shown that labor market reforms must be viewed not just in terms of the need to improve isolated institutions, but also in the context of their mutual interaction and in view of a country's economic model.

Economic literature posits various types of interactions between institutions. For example, it is assumed that if workers have to pay high taxes on labor, the motivation of the unemployed to find jobs will decrease. It is also assumed that high labor taxes can have a negative effect on creating new jobs because they simultaneously decrease labor force supply and demand. At the same time, it is believed that by increasing the costs of firing and hiring, strict employment protection discourages the creation of new jobs. This can in turn affect the intensity of job seeking among the unemployed, since the chances of finding a

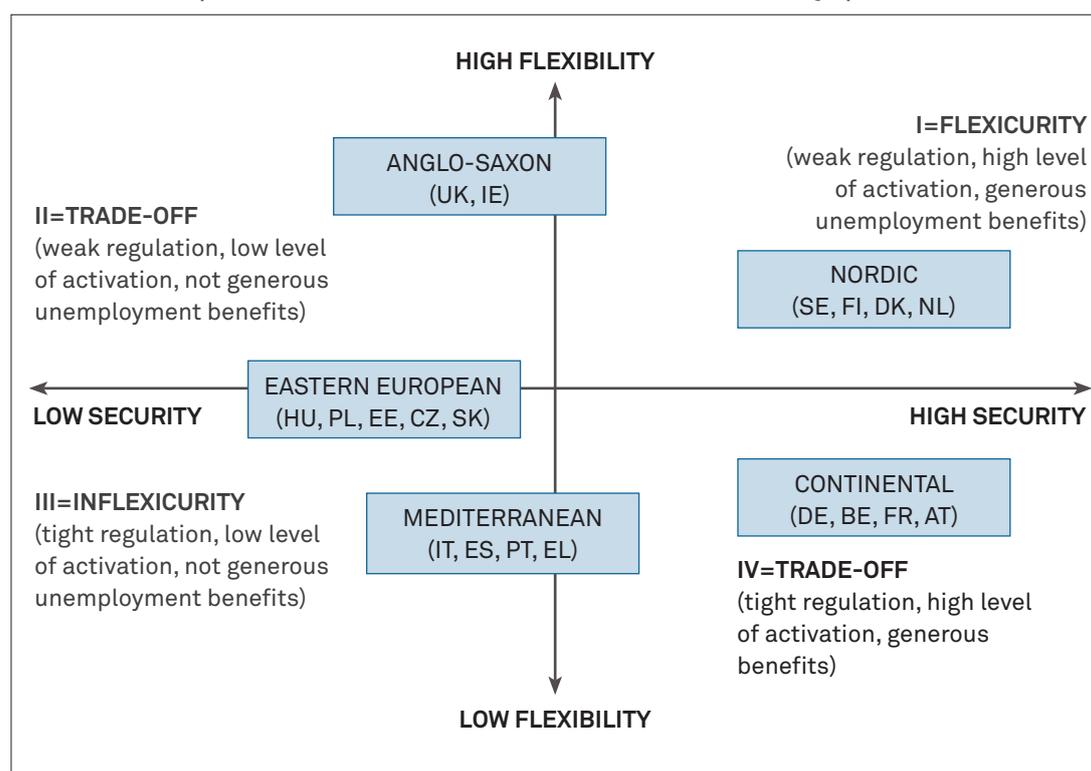
⁶⁶ Martin Schröder, "Integrating Welfare and Production Typologies: How Refinements of the Varieties of Capitalism Approach call for a Combination of Welfare Typologies," *Journal of Social Policy* 38, No. 1 (2009), p. 27.

job are smaller. Interactions between employment protection and unemployment benefits may have similar mutual effects. Strict employment protection potentially effects a decrease in new jobs, which can in turn be worsened by generous benefits that lower the motivation for job seeking. That is to say, interactions determine whether or not the effect of employment protection will be considerable when combined with other “institutional rigidities.”⁶⁷

Still, empirical studies have not reached a consensus on the effects of interactions between labor market institutions, but the implications of such interactions must be taken into account when designing labor market reforms.

Interactions between institutions are particularly prominent in the flexicurity debate. In their theoretical classification of flexicurity, Muffels and Wilthagen categorize EU states according to aspects of flexibility (high / low employment regulation) and security (generous / ungenerous benefits and high / low activation) (see Graph 2.2). Empirical research has so far largely confirmed this classification in practice.⁶⁸

Graph 2.2. Classification of states in the flexicurity quadrant



Source: Muffels and Wilthagen (2013)⁶⁹

⁶⁷ See, for example, an overview of the literature on these interactions in Avdagic and Salardi, “Tenuous link,” p. 747.

⁶⁸ Muffels and Wilthagen, “Flexicurity: A new paradigm,” p. 117.

⁶⁹ Adapted from: Muffels and Luijkx (2008), in: Muffels and Wilthagen, “Flexicurity: A new paradigm,” p. 117.

In the context of flexicurity, the idea is that labor market institutions complement each other to achieve the desired labor market performance;⁷⁰ however, Muffels et al. point out that only some states can achieve high levels of both mobility and security at the same time.⁷¹ Apart from implementation issues (e.g. lack of resources, lack of capacity),⁷² reforms are certainly affected by existing policies and achieved compromises: for example, many states with strict employment protection have less generous unemployment benefits schemes.⁷³ According to Boeri et al, an analysis of existing systems in 28 countries has shown that they represent very stable political-economic equilibriums, and that certain reforms, such as making employment protection flexible for permanent contracts, may be unfeasible.⁷⁴ Political support for far-reaching reforms is particularly difficult to achieve when there is resistance from insiders due to the segmentation of the labor market, as has been witnessed in some continental countries and countries of South Europe.⁷⁵ Other challenges pertain to specific historical legacies, legal traditions, systems of industrial relations within the state,⁷⁶ as well as general differences in the values pursued (such as, for example, economic security and equality).⁷⁷

Considerable emphasis is placed on the significance of the institute of collective bargaining in the implementation of any labor market reforms. According to Muffels and Wilthagen, constructive social dialogue at all levels is considered a key precondition for the development of integrated and balanced reform packages at the state and sectoral levels⁷⁸. Empirical research has shown that negotiations at multiple levels through a unique system of industrial relations, as in the case of Denmark, lead to more comprehensive and inclusive reforms.⁷⁹ According to the European Expert Group on Flexicurity, one of the conditions for implementing a successful flexicurity policy is constructive and productive social dialogue between social partners and the government.⁸⁰ The experience of some European countries that implemented labor market reforms in the 1990s have shown that managing unemployment is considerably facilitated

⁷⁰ Viebrock and Clasen, "Flexicurity and welfare reform," p. 312.

⁷¹ Ibid, p. 319; Muffels and Wilthagen, "Flexicurity: A new paradigm," p. 119.

⁷² Viebrock and Clasen, "Flexicurity and welfare reform," p. 320.

⁷³ Ibid, p. 313.

⁷⁴ Boeri et al. (2006) in Ibid, p. 313.

⁷⁵ Ibid, p. 320.

⁷⁶ Ibid, p. 319.

⁷⁷ Richard B. Freeman, "Single Peaked vs. Diversified Capitalism: The Relation Between Economic Institutions and Outcomes," Working Paper No. 7556 (NBER, 2000), p. 6.

⁷⁸ Muffels and Wilthagen, "Flexicurity: A new paradigm," p. 114.

⁷⁹ Ibid.

⁸⁰ Viebrock and Clasen, "Flexicurity and welfare reform," pp. 310 and 320.

in countries where social partners worked towards strong coordination and consensus building.⁸¹

The way in which similar institutions function in practice can be completely different from state to state, depending on their interaction with other institutions. For example, the introduction of fixed-term contracts in Spain in the 1980s led to substantial use of such contracts, but following the adoption of similar legislation in Germany, companies generally continued to employ apprentices on permanent contracts, which is linked to strong market coordination mechanisms characteristic for the German economy. On the other hand, countries with different regulatory policies and practices may have similar labor market performance.⁸² Given the degree to which labor market institutions constitute a unique and consistent system, it is clear that the effects of an institution cannot be easily extrapolated from one system into another, and that the possibility of “transplanting” a model from one country into another is questionable.⁸³ A unique or common approach to reforms in this realm is not likely to be successful,⁸⁴ and according to Freeman, it is not necessary for economic progress given that capitalism should be sufficiently robust to function equally efficiently in diverse contexts of labor market regulation without requiring unique, dominant labor market institutions.⁸⁵ It is precisely the specificities of the institutional environment of the labor market, and the way labor market institutions have evolved and are mutually configured, that make it difficult to draw definitive conclusions about which policies, in general, would be best suited to a given context.

The following chapters provide an overview of the most important labor market institutions in BiH in comparative perspective, in relation to their counterparts in other European countries.

⁸¹ Esping-Andersen and Regini, “Conclusions,” pp. 340–341.

⁸² Freeman, “Single Peaked vs. Diversified Capitalism,” pp. 8–9.

⁸³ *Ibid.*, p. 19.

⁸⁴ Muffels and Wilthagen, “Flexicurity: A new paradigm,” p. 119.

⁸⁵ Freeman, “Single Peaked vs. Diversified Capitalism,” p. 1.

3.

Labor Market Dynamics and Trends in Bosnia and Herzegovina

The BiH labor market suffers from numerous structural problems and shortcomings. The current organization of the labor market, combined with a generally unfavorable macroeconomic climate and other socio-economic factors, results in low levels of labor force absorption and so-called structural unemployment⁸⁶, which represents one of the key problems that BiH society faces in the post-war transition period.

The drop in economic activity in the past few years, resulting from the 2008 global financial crisis and the consequent long-lasting recession in most European countries, has further exacerbated and amplified the problems of the BiH labor market, which has shown itself to be inefficient in mediating the effects of the crisis and adapting to the newly established economic environment. In the years following the crisis, the problem of cyclical unemployment has also become increasingly prominent, which is manifested in a reduced demand for workers⁸⁷. Thus, it can be said that the BiH labor market is characterized by combined structural and cyclical unemployment. The effects of this situation are best illustrated by the fact that BiH is ranked among the European countries with the highest levels of unemployment.

According to the Agency for Statistics of BiH, in December 2014, the record showed 547.112 unemployed persons⁸⁸. In relation to the total labor force made up of all registered unemployed and formally employed persons in the country, according to the data of the Labor and Employment Agency of BiH, this makes the

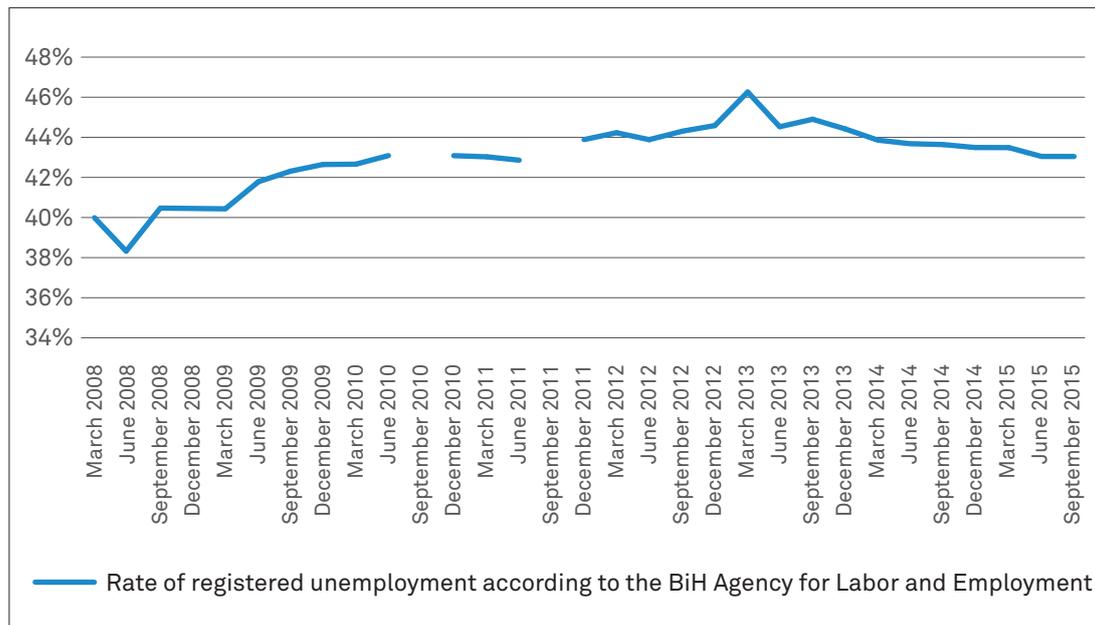
⁸⁶ Structural unemployment is a form of unemployment caused by “mismatched supply and demand for workers in terms of occupation, education and qualifications or their regional distribution” and, as such, “this type of unemployment requires long-term and active measures in order to be reduced or removed” – definition taken from GEA – Center for Research and Studies, *Nezaposlenost u BiH: (Ne)efikasnost postojećeg tržišta rada* [Unemployment in BiH: (In)efficiency of the Current Labor Market] (Banja Luka: GEA, 2008), p. 41.

⁸⁷ Cyclical unemployment is a form of unemployment that arises “in the situation when total demand for labor is low due to a decrease in aggregate demand for products and services caused by a drop in economic activity and recession” – definition taken from: GEA - Center for Research and Studies, *Osnovni mehanizmi tržišta rada* [Basic Mechanisms of the Labor Market] (Banja Luka: GEA, 2008), p. 61.

⁸⁸ Agency for Statistics of BiH, Saopštenje: registrovana nezaposlenost u decembru 2014. [Release: Registered Unemployment in December 2014] (Sarajevo: BiH Agency for Statistics, 2015).

registered unemployment rate amount to 43.6%⁸⁹. Even though when compared with the same months in the preceding three years, a slight decrease in the registered unemployment rate can be discerned (in 2013 = 44.5%, in 2012 = 44.5%, and in 2011 = 43.8%), it is still greater by 3 percentage points than it was in December 2008, when the first impacts of the world economic crisis were felt in the domestic economy and labor market. Despite an increase at the start of the year, the trend of slight decrease in the registered unemployment rate, with some fluctuation, has continued into 2015, reaching 43% in September⁹⁰.

Graph 3.1. Registered unemployment rate in BiH (2008–2015)



Source: Labor and Employment Agency⁹¹

Given the high proportion of the grey economy and employment in the informal labor market in BiH,⁹² in addition to the assumption that many persons register with employment services in order to be eligible for health insurance,⁹³ data

⁸⁹ “Pregled stanja tržišta rada na dan 31. januara 2015. godine” [Labor Market Situation Overview on 31 January 2015], Labor and Employment Agency of BiH, 4 March, 2015, <http://www.arz.gov.ba/statistika/mjesečni/default.aspx?id=1775&langTag=bs-BA> (accessed on 25 July 2015).

⁹⁰ “Pregled stanja tržišta rada na dan 31. januara 2015. godine” [Labor Market Situation Overview on 31 January 2015], Labor and Employment Agency of BiH, 4 March, 2015, <http://www.arz.gov.ba/statistika/mjesečni/default.aspx?id=1775&langTag=bs-BA> (accessed on 25 July 2015).

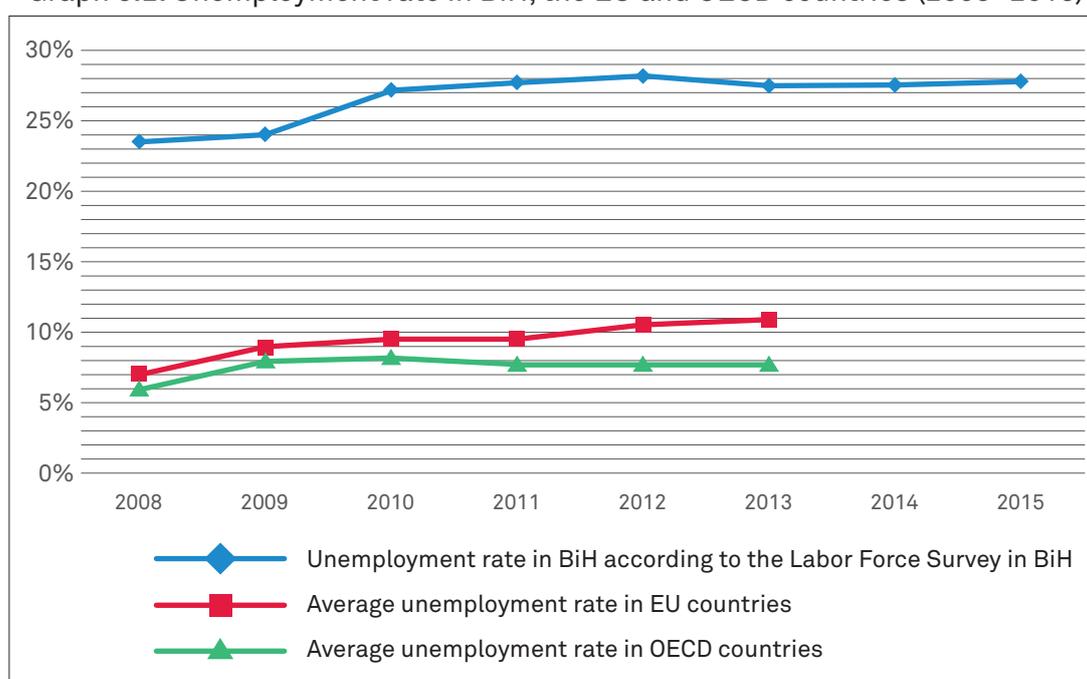
⁹¹ Monthly releases of the Labor and Employment Agency available on their website: http://www.arz.gov.ba/statistika/mjesečni/Archive.aspx?langTag=bs-BA&template_id=152&pageIndex=1 (accessed on 17 December 2015).

⁹² According to ILO estimates, the share of those employed informally accounted for around 23% of the total number of employed in BiH in 2013. International Labor Organization (ILO), *Global Employment Trends 2013* (Geneva: ILO, 2013), p. 60.

⁹³ International Labor Organisation (ILO), *BiH: Decent Work Country Programme Document, 2012–2015* (2012), p. 2.

on registered unemployment should be taken with reservation, because it does not offer insight into the actual state of unemployment. The annual labor force survey, conducted by the Agency for Statistics of BiH in cooperation with the Federal Institute for Statistics and the Institute for Statistics of Republika Srpska, provides more credible data in this respect. The labor force survey (LFS) is an internationally recognized instrument for gathering comparable data on the working-age population and the total labor force of a country, i.e. data on “three main, mutually exclusive, contingents of population: the employed, the unemployed and inactive persons”⁹⁴. According to LFS findings, the unemployment rate in 2014 was 27.5%⁹⁵ – which is by about 16 percentage points lower than the average registered unemployment rate in the same year – while the preliminary findings for 2015 indicate that the surveyed unemployment rate has increased to 27.7%⁹⁶. Compared to 2008, the surveyed unemployment rate in 2015 is greater by 4.3 percentage points.

Graph 3.2. Unemployment rate in BiH, the EU and OECD countries (2008–2015)



Sources: Labor force surveys in BiH (2008-2015) and World Bank data⁹⁷

⁹⁴ BiH Agency for Statistics, Anketa o radnoj snazi: 2013 [Labor Force Survey: 2013] (Sarajevo: BiH Agency for Statistics, 2013), p. 6.

⁹⁵ BiH Agency for Statistics, Anketa o radnoj snazi: 2014 [Labor Force Survey: 2014: Final Results] (Sarajevo: BiH Agency for Statistics, 2014), p. 31.

⁹⁶ BiH Agency for Statistics, Anketa o radnoj snazi: 2015: prethodni podaci [Labor Force Survey: 2015: preliminary results] (Sarajevo: BiH Agency for Statistics, 2015), p. 2.

⁹⁷ “Unemployment, total (% of total labor force) (modelled ILO estimate),” World Bank, <http://data.worldbank.org/indicator/SL.UEM.TOTL.ZS/countries/EU-OE?display=graph> (accessed on 25 October, 2015).

Even though due to the effects of the economic crisis, the last few years have seen a significant increase in unemployment compared to 2008, the continuously high unemployment rate throughout the past two decades indicates serious structural problems in the labor market. Thus, for example, in 2006, the survey unemployment rate was 31.1%, while in 2007 it was lower by 2.1 percentage points or 29.0%. In both years, although real GDP growth in BiH was around 6%, the annual survey unemployment rate was somewhat higher than it was in the period from 2008 to 2015⁹⁸. In other words, the unemployment rate remained high despite positive macroeconomic trends in the segment of economic growth, which is a common feature of transition economies in the Western Balkans.⁹⁹ According to an analysis of the International Labor Organization for BiH, the reasons for a poor outlook on employment could be found “in the slow pick up of economic activities after the war and the massive lay-offs following privatization of the state-owned companies. Even though a significant increase in economic activity was recorded from 2005 to 2008, it was not sufficient to counterbalance the losses of employment resulting from structural adjustments.”¹⁰⁰

When it comes to the employment rate,¹⁰¹ according to the preliminary results of the LFS for 2015,¹⁰² it is at 31.9%, which is a slight increase compared to 2014, when it was 31.7%¹⁰³. Still, if we consider the employment data from 2008 on in perspective, an initial drop is seen from 2008 to 2011, followed by stagnation of the employment rate, which in 2015 is still 1.7 percentage points below what it was in 2008.¹⁰⁴

⁹⁸ For an overview of real GDP growth from 2002 to 2008, i.e. in the years preceding the economic crisis, see: BiH Central Bank, “Tržište kapitala: Pregled sadašnje ekonomske situacije u BiH” [Capital Markets: Synopsis of the Current Economic Situation in BiH], <http://cbbh.ba/index.php?id=702&lang=hr> (accessed on 25 October, 2015).

⁹⁹ Kovtun et al, “Boosting Job Growth in the Western Balkans,” Working Paper WP/14/16 (IMF, 2014), p. 6; and Ognjen Đukić and Miroslav Tomić, *Kako do nižeg oporezivanja rada bez štete za javne fondove?* [How to achieve lower labor taxation without harming public funds?](Banja Luka: GEA, 2013), p. 6.

¹⁰⁰ ILO, BiH: Decent Work Country Programme Document, p. 2.

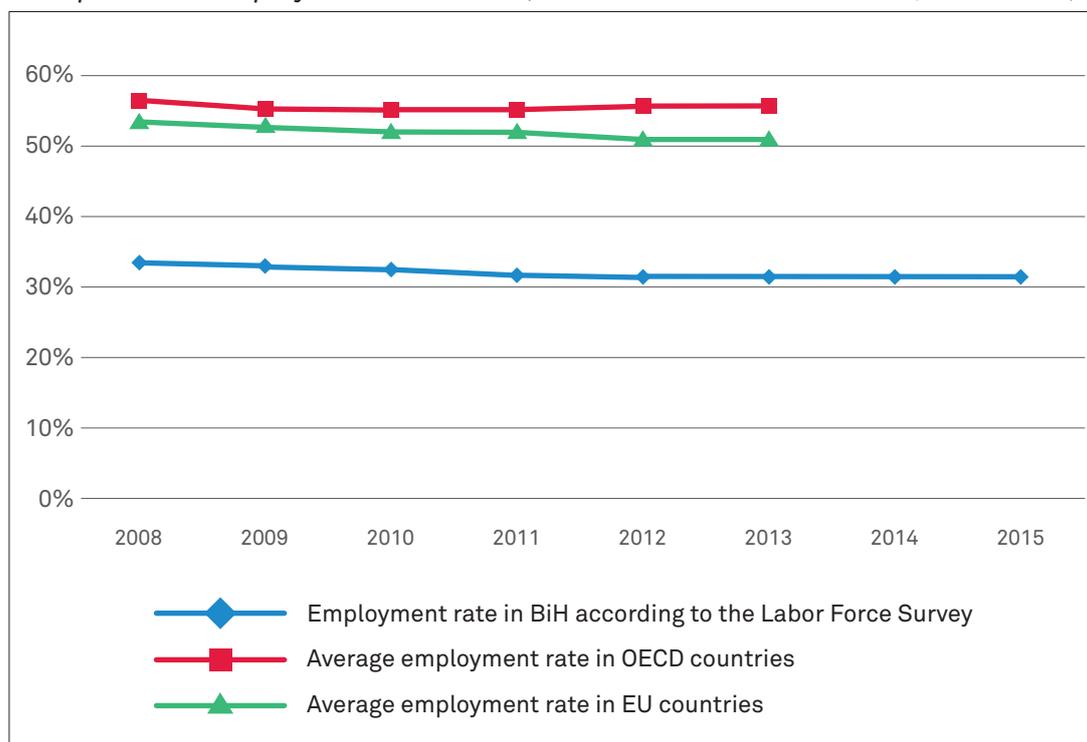
¹⁰¹ The employment rate is calculated as the ratio of persons employed to the total working age population (employed / working age population x 100). BiH Agency for Statistics, Labor Force Survey: 2014, p. 21.

¹⁰² BiH Agency for Statistics, Labor Force Survey: 2015, p. 2.

¹⁰³ BiH Agency for Statistics, Labor Force Survey: 2014, p. 31.

¹⁰⁴ LFS data for these years available on the website: http://www.bhas.ba/?option=com_content&view=article&id=113=ba (accessed on 25 October, 2015).

Graph 3.3. Unemployment rate in BiH, the EU and OECD countries (2008–2015)



Sources: Labor force surveys in BiH (2008 - 2015) and World Bank data¹⁰⁵

The labor market in BiH is also characterized by low participation of the working age population (age 15 and above) in the labor market with the activity rate in the period from 2007 to 2014 ranging from 43.6% to 44.6%.¹⁰⁶ According to preliminary survey results for 2015, it was at 44.1%,¹⁰⁷ which is the lowest activity rate in the Western Balkans (except for Kosovo). Within the same years, the activity rate in OECD countries was around 60% and around 57.5% in countries of the EU.¹⁰⁸

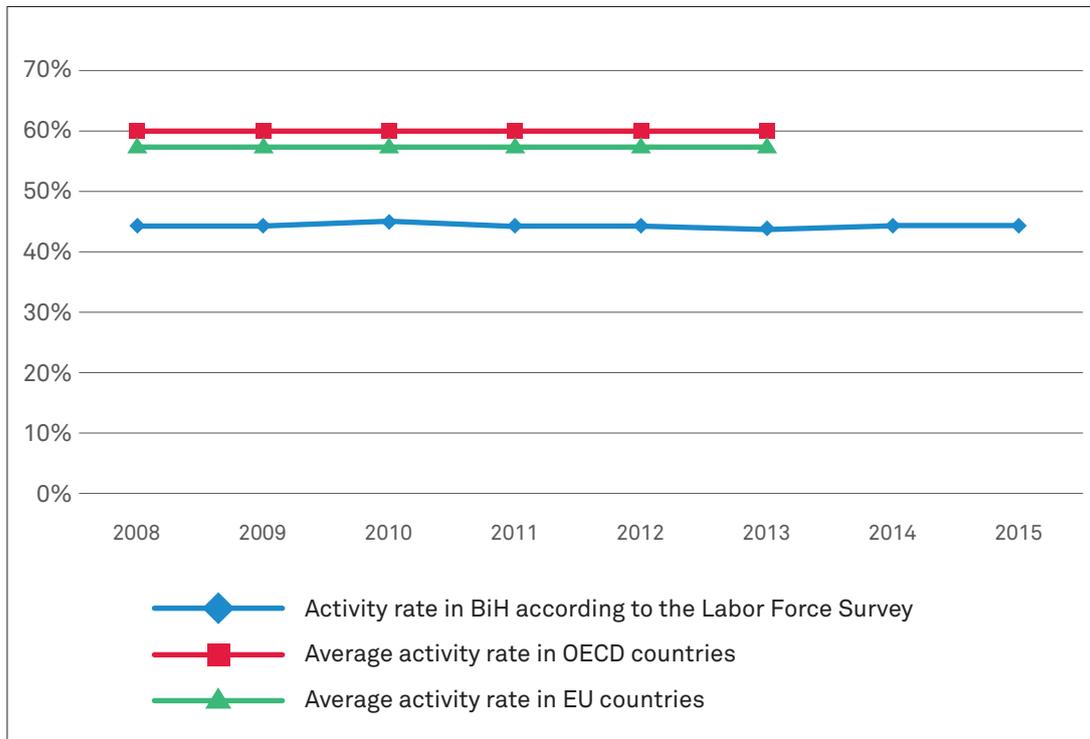
¹⁰⁵ “Employment to population ratio, 15+, total (%) (modelled ILO estimate),” World Bank, <http://data.worldbank.org/indicator/SL.EMPTOTL.SP.ZS/countries/OE-EU?display=graph> (accessed on 25 October, 2015).

¹⁰⁶ See labor force surveys for these years, as well as Labor and Employment Agency, *Employment Strategy in Bosnia and Herzegovina 2010–2014*, 2010, p. 7.

¹⁰⁷ BiH Agency for Statistics, Labor Force Survey: 2015, p. 2.

¹⁰⁸ “Labor force participation rate, total (% of total population ages 15+) (modelled ILO estimate),” World Bank, <http://data.worldbank.org/indicator/SL.TLF.CACT.ZS/countries/OE-EU?display=graph> (accessed on 25 October, 2015).

Graph 3.4. Rate of activity in BiH, the EU and OECD countries (2008–2015)



Sources: Labor force surveys in BiH (2008 - 2015) and World Bank data¹⁰⁹

In addition, BiH has a very high rate of youth unemployment, the highest among European countries. In 2014, the youth (age 15–24) unemployment rate in BiH was 62.7%,¹¹⁰ while, for the sake of comparison, average youth employment in the EU 28¹¹¹ for that same year was 22.2%,¹¹² and the average for Western Balkan countries¹¹³ was 48.70%.¹¹⁴ Although youth unemployment is recognized as one of the key socio-economic problems, BiH authorities have not invested significant efforts to overcome it in the previous period.¹¹⁵

¹⁰⁹ Ibid.

¹¹⁰ BiH Agency for Statistics, Labor Force Survey: 2014, p. 37.

¹¹¹ Applies to all EU member states.

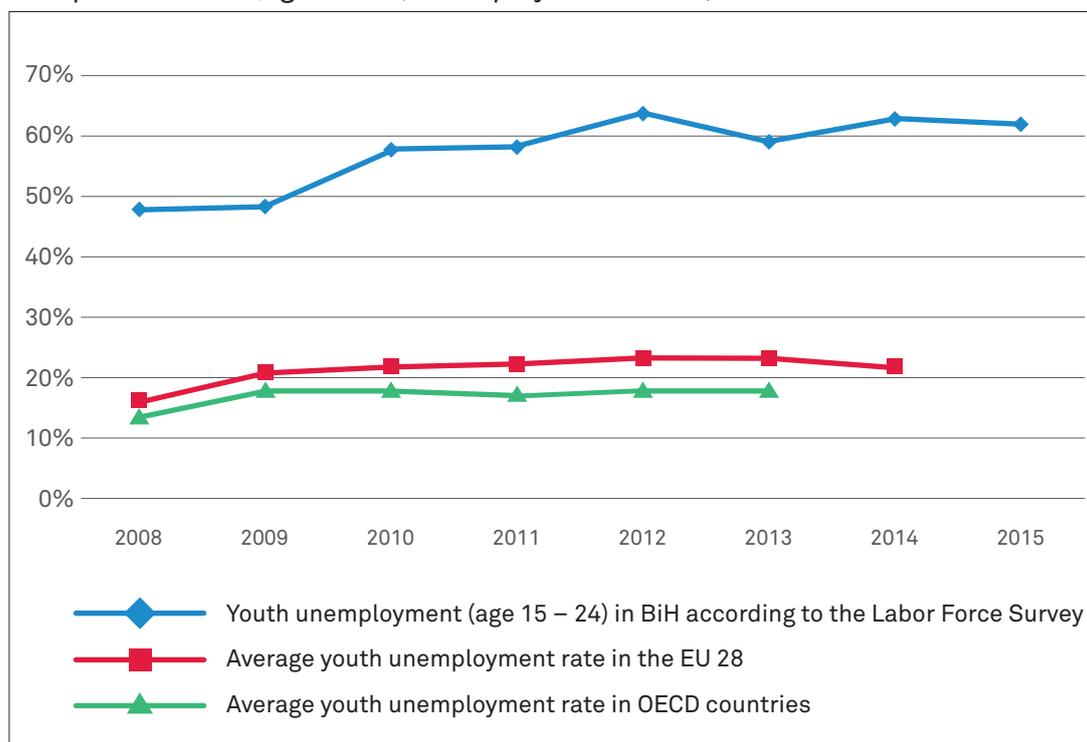
¹¹² “Unemployment statistics,” EUROSTAT, http://ec.europa.eu/eurostat/statistics-explained/index.php/Unemployment_statistics (accessed on 25 October, 2015).

¹¹³ Non-weighted average.

¹¹⁴ Calculation by the authors based on data from 2014 labor force surveys in Western Balkan countries.

¹¹⁵ See Erol Mujanović, *Nezaposlenost mladih u Bosni i Hercegovini: trenutna situacija, izazovi i preporuke* [Youth Unemployment in Bosnia and Herzegovina: Current Situation, Challenges and Recommendations] (Sarajevo: Friedrich-Ebert-Stiftung, 2013), pp. 7–13.

Graph 3.5. Youth (age 15–24) unemployment in BiH, the EU and OECD countries



Sources: Labor force surveys in BiH (2008–2015), World Bank¹¹⁶ and EUROSTAT¹¹⁷ data

Another worrisome trend is the continuously high share of the long-term unemployed in the total number of persons unemployed: 84.7% of the unemployed have been looking for work for a year or longer (of which over a half are persons who have been looking for work for five years or longer),¹¹⁸ as opposed to the average of 49.3% of long-term unemployed (over one year) in the overall unemployed population in the EU 28 in 2014.¹¹⁹ According to a report by the European Commission and the Vienna Institute for International Economic Studies (2008), the assumption is that high long-term unemployment rates in Balkan countries do not generally provide complete insight into the labor market due to significant labor flows between the informal sector, employment and unemployment.¹²⁰

¹¹⁶ “Unemployment, youth total (% of total labor force ages 15-24) (modelled ILO estimate),” World Bank, <http://data.worldbank.org/indicator/SL.UEM.1524.ZS/countries/OE?display=graph> (accessed on 25 October, 2015).

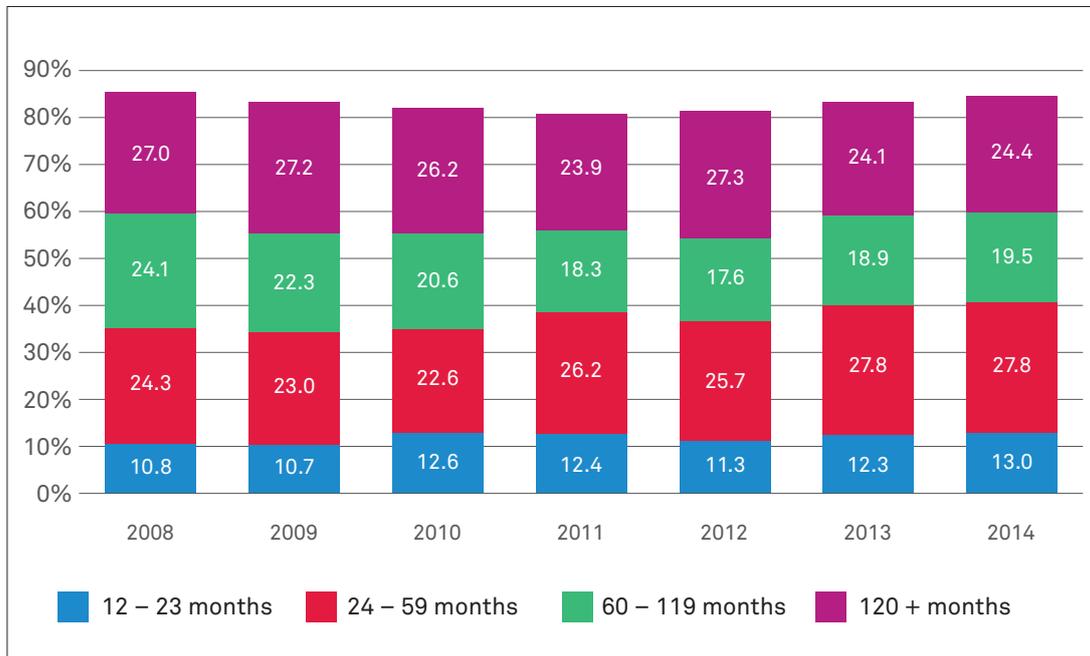
¹¹⁷ “Unemployment rate EU-28 2005–2014,” EUROSTAT, http://ec.europa.eu/eurostat/statistics-explained/index.php/File:Unemployment_rate_EU-28_2005-2014.PNG (accessed on 25 October, 2015).

¹¹⁸ BiH Agency for Statistics, Labor Force Survey: 2014, p. 59.

¹¹⁹ “Unemployment statistics,” EUROSTAT, http://ec.europa.eu/eurostat/statistics-explained/index.php/Unemployment_statistics_at_regional_level (accessed on 25 October 2015).

¹²⁰ DG for Economic and Financial Affairs and Vienna Institute for International Economic Studies, Adjustment capacity of labour markets of the Western Balkan countries, Economic Papers 346 (2008), p. 40.

Graph 3.6. Long-term unemployment rates in BiH according to the Labor Force Survey

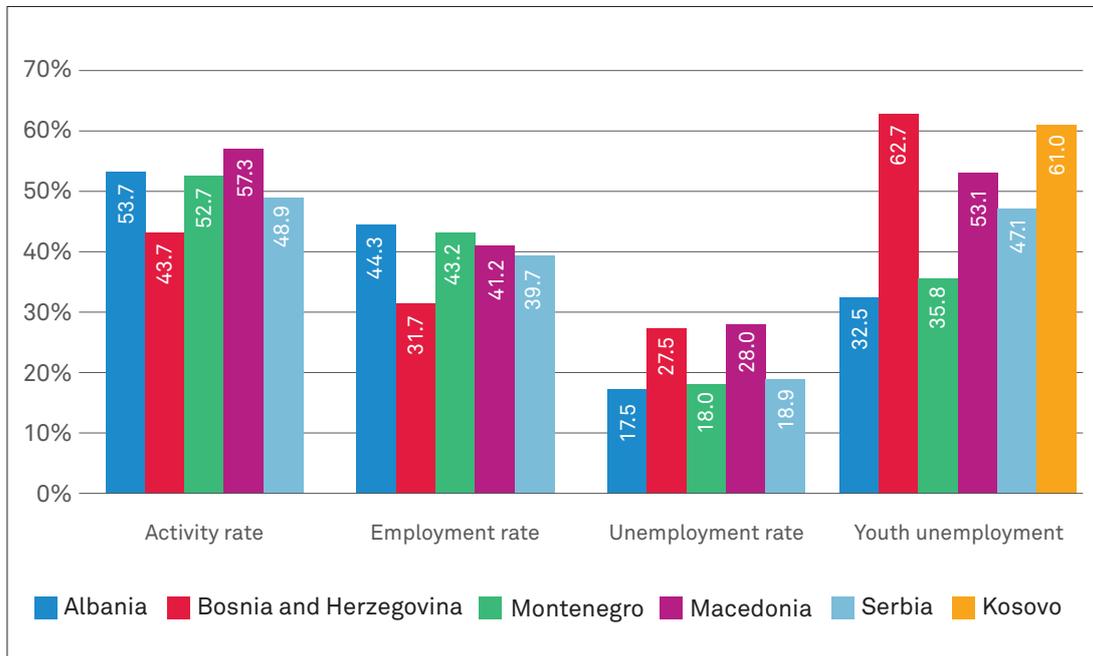


Sources: Labor force surveys in BiH (2008 - 2015)

If we compare basic labor market indicators among Western Balkan countries (except for Kosovo) in 2014, it can be concluded that they are least favorable in BiH. Thus, the activity rate of the working-age population in BiH is considerably below the average for the Western Balkans, which is 51.26%, while the employment rate is similarly almost 9 percentage points below the 40.02% Western Balkans average. Although the surveyed unemployment rate is somewhat higher in Macedonia compared to BiH, it is in BiH still around 5.5 percentage points above the regional average (21.98%). Finally, another concern is the continuously high youth unemployment, which was 14 percentage points above the regional average in 2014.¹²¹

¹²¹ All data taken from labor force surveys published on the following websites: Albania: <http://www.instat.gov.al/en/themes/labour-market.aspx> (accessed on 17, December 2015); BiH: http://www.bhas.ba/ankete/LFS_2014_001_01_hr.pdf (accessed on 17 December, 2015); Montenegro: <http://monstat.org/userfiles/file/ars/2014/ARS%20-%20Godisnje%20saopstenje,%202014.pdf> (accessed on 17 December, 2015); Macedonia: <http://www.stat.gov.mk/Publikacii/2.4.15.04.pdf> (accessed on 17 December, 2015); Serbia: http://webrzs.stat.gov.rs/WebSite/repository/documents/00/01/71/73/SB-593-bilten_ARS_2014.pdf (accessed on 17 December 2015); Kosovo: https://ask.rks-gov.net/ENG/publikimet/doc_view/1314-results-of-the-kosovo-2014-labour-force-survey?tmpl=component&format=raw (accessed on 17 December, 2015).

Graph 3.7. Comparative overview of basic labor market and youth unemployment indicators in Western Balkan countries (excepting Kosovo) in 2014



Sources: Labor force surveys for 2014

4.

Labor Market Institutions in BiH in a Comparative Perspective

According to the 2015–2016 Global Competitiveness Index, BiH ranks 131st in terms of labor market efficiency.¹²² Labor market analyses have most frequently identified the following causes of labor market inefficiency in BiH: rigid labor legislation, high taxation of labor, inadequate employment policies, insufficient development of human potential, and incompatibility of education policies with labor market demands. Furthermore, it is believed that the social dialogue institute is underdeveloped, which reduces possibilities for coordination between the economy and the labor market and reaching a compromise between labor and capital.

Due to the inability to stimulate growth and employment within the existing institutional framework in a satisfactory manner, the labor market has recently become the focus of initiatives and debates on socio-economic reforms in BiH. A significant portion of the measures from the 2015 National Economic Reform Program (NERP)¹²³ pertains to the labor market. Due to obligations towards the IMF as part of the *stand-by* arrangement,¹²⁴ authorities in BiH have placed labor market reforms high on the agenda, and the requirement to reform the labor market is part of the official EU policy towards BiH, articulated in the initiative “Compact for Growth and Jobs.”¹²⁵ The BiH 2015–2018 Reform Agenda foresees that the entity governments, with the assistance from the World Bank and the IMF, will change their labor laws. In FBiH, the new Labor Law was adopted in late July 2015 through expedited parliamentary procedure and with the opposition of the FBiH Federation of Independent Trade Unions, while changes to labor legislation in the RS and the Brčko District (BD) are pending.

To better understand the situation of the labor market in BiH, especially in view of the dominant explanations for the cause of the problems it faces, and to situate the proposed reforms and their implications into a wider institutional framework

¹²² For more, see Klaus Schwab, *The Global Competitiveness Report 2015–2016* (Geneva: World Economic Forum, 2015), p. 12.

¹²³ See Council of Ministers of BiH, *National Economic Reform Programme for 2015*.

¹²⁴ The *stand-by* arrangement between IMF and BiH expired in 2015. Cooperation between IMF and BiH is expected to continue in 2016.

¹²⁵ See EU Delegation to BiH, *Compact for Growth and Jobs in BiH*; and EU Delegation to BiH, “Forum for Prosperity and Jobs in Bosnia and Herzegovina,” 28 May 2014.

and consider them in comparison with the experiences of other countries, this chapter presents an overview of the main BiH labor market institutes in comparative perspective: (1) employment protection legislation, (2) costs of labor, (3) social dialogue and collective bargaining, and (4) employment policy, which together with the education and training systems and the macroeconomic policy and climate, determine the dynamics and the efficiency of the labor market.

4.1. Employment Protection Legislation

4.1.1. Definitions and key aspects of employment protection legislation

Employment protection legislation (hereinafter: EPL) comprises rules in the form of laws, collective agreements and court judgements protecting workers from arbitrary lay-offs and income fluctuation. EPL usually regulates termination of full-time employment, fixed-term employment and collective lay-offs.¹²⁶ In its 2013 report, the OECD provides an overview of the key aspects of EPL in OECD and EU countries,¹²⁷ which are given below.

When it comes to defining dismissal, the rules usually determine valid reasons for termination, which may be personal (e.g. conduct, capabilities of the employee) and economic circumstances (e.g. decrease in company revenues).¹²⁸ Meanwhile, definitions of unfair dismissal vary considerably. For example, in Spain, only in cases of unfitness or inability to adapt to technological change may worker capability be sufficient ground for dismissal. The law in Norway allows for dismissals for personal motives, but these reasons have been restricted by courts to cases that pertain to material breach of employment contract, such as disloyalty or continuous absenteeism. When it comes to economic redundancy, in many countries (e.g. Estonia, France, Germany, Italy, Norway and Sweden), dismissals may be considered unfair if a worker considered redundant could have been reallocated to another position in the same company. In almost one half of OECD countries, worker capability and redundancy are considered to be fair grounds for dismissal, with no further or with limited additional substantive conditions.¹²⁹

The rules usually stipulate a legal remedy in the event of unfair dismissal. In many countries, if the dismissal is ruled to be unfair by the court, the judge can order the worker to be reinstated, and the reinstated employee is typically

¹²⁶ Sandrine Cazes, Sameer Khatiwada and Miguel Malo, *Employment Protection and Collective Bargaining: Beyond the deregulation agenda*, Employment Working Paper No. 133, ILO, (2012), p. 23.

¹²⁷ OECD, *Employment Outlook 2013*, pp. 79–103.

¹²⁸ Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, pp. 2–3.

¹²⁹ OECD, *Employment Outlook 2013*, p. 81.

entitled to a compensation of salary and benefits.¹³⁰ In a number of European countries, this option is offered to workers (e.g. Austria, the Czech Republic, and also in Portugal, except for cases of procedural irregularity), but in most countries, it is not an option (rather, the employer may choose to pay the worker compensation), unless workers were dismissed on the basis of grounds that are explicitly prohibited, such as discrimination (e.g. Estonia, Belgium, Luxembourg, France, Spain, Switzerland, and Nordic countries, except for Denmark and Norway).¹³¹

Minimum notice periods, as well as severance pay for employees with longer seniority are foreseen in most OECD countries and in all EU countries. Also, in almost all OECD countries, there is an obligation to inform the worker in writing and often to justify the dismissal. In some countries (e.g. Germany, and for union members in Slovenia and Latvia), this letter takes effect following authorization by a relevant authority or by court decision. In many countries, the employer is obliged to inform the union or workers council, and/or the employment service or other public authorities about a dismissal, and some even require negotiations with the unions for a decision on dismissal to become final, especially in cases of redundancy.¹³²

There are usually special rules for collective dismissals, which pertain to the number of workers that may be dismissed (depending on the size of the company, usually more than five) within a certain period (on average in the course of a month in OECD countries). Given the wider economic and social implications of collective dismissals, the conditions are usually more rigid than those for individual dismissals.¹³³ There is usually an obligation to notify the union/workers' council or an employment service and/or to negotiate with unions (e.g. in Belgium, Hungary, Ireland, Sweden, Switzerland). Especially in the countries of the EU, companies may be obliged to adopt a social plan that typically contains measures for reemployment, training, outplacement services, and in some cases, additional compensation.¹³⁴

When it comes to using standard, fixed-term contracts, only some OECD countries (e.g. Estonia, France, Greece and Norway, among European countries) require that employing workers on fixed-term contracts must be justified by an "objective" or "material" situation (e.g. for activities of limited duration); otherwise, the use of such contracts is justified by the needs of the employer or employee, and in more than half the OECD countries, no justification is necessary, at least not for the first such contract. The number of contract renewals and/

¹³⁰ In the EU, typical compensation for unfair dismissal of an employee with 20 or more years of job tenure are highest in Sweden (32 months), Italy (around 21 months), Portugal (17.5 months), and France (16 months), and lowest in Estonia and Poland. *Ibid*, p. 82.

¹³¹ *Ibid*, p. 82.

¹³² *Ibid*, p. 80.

¹³³ Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, pp. 2–3.

¹³⁴ OECD, *Employment Outlook 2013*, p. 86.

or successive assignments in the same company is usually limited. In some countries, even if there are no restrictions, courts may treat the use of these contracts as permanent employment (e.g. Denmark, Finland, Norway and Switzerland), and the legal remedy may be paying damages to the worker or change of contract.¹³⁵

Laws also regulate the procedures for employing workers through temporary work agencies.¹³⁶ This is where workers, through an agency, temporarily work for a company, usually on tasks that fall outside of the company's main line of business. Workers in such arrangements usually receive training and support in finding new assignments. In some countries, agencies may have open-ended contracts with workers and may pay them a low wage between fixed-term assignments (e.g. in Austria, Italy, Slovenia, Sweden). Given that this type of work is susceptible to abuse, rules stipulate equal treatment of workers, agency licensing and regular reporting requirements, the types of assignments available for contracting, and the number of renewals and maximum cumulative duration of assignments. Owing to the EU Directive on temporary agency work, member states must guarantee equal wages and working conditions to agency workers as to permanent staff; however, in some countries, rules on equal treatment only apply to assignments exceeding a certain duration, or they guarantee minimum wages or working conditions.¹³⁷

4.1.2. Key Discussions, European Employment Protection Trends and Practices

Although it protects workers, the dominant opinion is that EPL limits the ability to adapt to changes in technology and demand and negatively impacts the creation of new jobs because employers are reluctant to employ new workers for fear of not being able to dismiss them easily.¹³⁸ Still, more stringent EPL should also be able to maintain employment through a crisis and encourage investments in the labor force.¹³⁹

¹³⁵ Ibid, p. 87-88.

¹³⁶ There are also other atypical temporary arrangements, such as self-employment, project work, etc. Ibid, p. 92.

¹³⁷ Ibid, p. 89-91.

¹³⁸ See, for example, Addisson and Texeira (2003) in: Avdagic and Salardi, "Tenuous link," p. 745.

¹³⁹ See for example Estevez-Abe et al. (2001) in: Avdagic and Salardi, "Tenuous link," p. 745.

However, the total impact of EPL on unemployment is theoretically uncertain because it depends on a multitude of economic variables.¹⁴⁰ Numerous authors, as well as organizations such as the OECD,¹⁴¹ indicate that research so far has not offered reliable proof for the assumption of negative impact of EPL on aggregate employment and unemployment rates¹⁴². Among other things, authors have indicated the problem of data, given that comparable quantitative measures of EPL are still imprecise, and that it is very difficult to measure the degree of flexibility of EPL given the lack of unique indicators.¹⁴³

There are other assumptions about the effects of EPL on the labor market. For example, the assumption of negative impact on labor force mobility has mostly been confirmed by research, indicating that overly rigid regulations may decrease labor force fluctuations and transitions between jobs and from unemployment to employment.¹⁴⁴ This means that the unemployed have a harder time finding jobs, which can particularly affect groups such as youth, women and low-skilled workers.¹⁴⁵ Theory also foresees that EPL can reduce productivity and innovation,¹⁴⁶ although some authors also claim that, through investments

¹⁴⁰ According to Bertola (1992), it may depend on the functional form of the labor force demand function, the discount rate, labor force fluctuations or wage flexibility. In: Avdagic and Salardi, "Tenuous link," p. 745. Similarly, given that EPL may have different effects on the costs of labor, employment and productivity – some positive, and some negative – other authors claim that the net impact of the effects of EPL depends most probably on the size of companies and type of activities, as well as on economic circumstances. Cazes, Sandrine and Alena Nesporova, "Introduction," in *Flexicurity: A Relevant Approach in Central and Eastern Europe*. Ed. Sandrine Cazes i Alena Nesporova (Geneva: ILO, 2007), p. 3.

¹⁴¹ OECD, *Employment Outlook 2004* (Paris: OECD, 2004), p. 81; OECD, *Employment Outlook 2013*, p. 71.

¹⁴² These are usually cross-country or time-series analyses of statistical data. See, for example: OECD, *Employment Outlook 2004*; and OECD, *Employment Outlook 2013*; Freeman, "Labor market institutions without blinders"; Freeman "Labor market institutions around the world," p. 22. See also: Bertola, Boeri and Cazes, 2000, in: Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, p. 2. For a few exceptions, see OECD, *Employment Outlook 2013*, p. 71.

¹⁴³ OECD *Indicators of Employment Protection* are most often used to measure EPL, but they are not considered to be complete indicators, given that they are mostly based on laws, whereas it is information about the implementation of laws in practice that is key for understanding the labor market, and especially labor force flows. This is considered particularly pertinent in developing countries that have strict EPL, but also have a large informal sector where *de jure* rules do not apply. Apart from that, some components of the indicators cannot be precisely measured (e.g. interpretation of just cause for dismissal), so the recommendation is to compensate for the subjectivity of indicators by analyzing the relationship with other institutions in order to better understand the impact of EPL on labor markets. Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, pp. 2–3.

¹⁴⁴ For a detailed overview of research, see OECD, *Employment Outlook 2013*, pp. 69–72.

¹⁴⁵ Esping-Andersen and Regini, "Conclusions," p. 337; OECD, *Employment Outlook 2004*.

¹⁴⁶ For a detailed overview of different models in this domain, see OECD, *Employment Outlook 2013*, p. 70.

in the labor force, EPL could improve productivity.¹⁴⁷ Recent studies have shown that stricter EPL has the tendency to reduce multi-factor productivity, but the relationship between EPL and innovation is less certain.¹⁴⁸ Research findings also suggest that stricter EPL may slow down adjustment to economic shocks.¹⁴⁹

An important discussion pertains to the impact of EPL on labor market duality. Some authors believe that strict EPL contributes to the widening of the gap between insiders and outsiders on the labor market,¹⁵⁰ because if fixed-term contracts are made flexible and strict regulations are retained for permanent employment, companies will replace permanent with temporary positions.¹⁵¹ According to the findings of some studies, *ceteris paribus*, strict protection of permanent employment encourages the use of temporary contracts.¹⁵² It is thought that great asymmetry in the degree of protection (and sometimes also the tax wedge) between permanent and temporary employment may reduce the rate of conversion of temporary contracts into permanent contracts, which hampers transitioning into a permanent employment relationship.¹⁵³ Case studies from Spain have shown that partial flexibilization has led to increased use of temporary contracts and reduced use of permanent contracts, and that low rates of transition between these two types of employment were the result of a regulatory gap.¹⁵⁴

Still, the analysis by Cazes et al. questions the presumption of a linear relationship between the duality of the labor market and EPL rigidity, given that it shows how a positive association is valid only in the case of extreme differences in strictness between temporary and permanent employment, suggesting that flexibilization would not necessarily lead to a systematic decrease in labor market duality.¹⁵⁵ Even reforms of partial flexibilization can, to a certain degree, be considered responsible for the expansion of non-permanent types of employment. Although other factors make it difficult to prove a significant relationship between regulatory change and the stock of the labor force on

¹⁴⁷ Ibid, p. 70. See also Viebrock and Clasen, "Flexicurity and welfare reform," pp. 311–312.

¹⁴⁸ See OECD, *Employment Outlook 2013*, p. 73.

¹⁴⁹ For more see OECD, *Employment Outlook 2013*, p. 71. See also Avdagic and Salardi, "Tenuous link," pp. 747–748.

¹⁵⁰ E.g. Boeri et al. (2003) in: Viebrock and Clasen, "Flexicurity and welfare reform," p. 311.

¹⁵¹ In such a scenario, there may also be an increase in wage pressure and unemployment, because insiders could demand higher pay without great risk of losing their jobs, and any negative repercussions on employment could be borne by outsiders. See, for example, Boeri and Garibaldi (2007), Bentolila et al. (2008), Bentolila and Dolado (1994) in: OECD, *Employment Outlook 2013*, p. 69.

¹⁵² For an overview of various research, see OECD, *Employment Outlook 2013*, pp. 72–73.

¹⁵³ For an overview of research, see OECD, *Employment Outlook 2013*, pp. 72–73.

¹⁵⁴ For an overview of studies, see Ibid, pp. 72–73.

¹⁵⁵ Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, p. 15.

temporary contracts,¹⁵⁶ statistical analyses provide certain limited evidence that, conditional on employment protection for permanent employees, lessening restrictions on temporary contracts has led to a greater share of non-permanent employees in new jobs.¹⁵⁷

Concerning trends related to statutory protection of employment in the form of laws, collective agreements and case law in Europe, it is clear that Europe is far from being a homogeneous whole. For example, employment protection legislation in continental Europe is, on average, more stringent than in Anglo-Saxon countries; in Denmark and Switzerland, employment protection is significantly weaker than in Belgium and France.¹⁵⁸ Still, by passing the *Directive on fixed-term work*,¹⁵⁹ the *Directive on part-time work*¹⁶⁰ and the *Directive on collective redundancies*,¹⁶¹ the EU adopted minimum standards in this area, which led to the approximation of rules among its member states.

¹⁵⁶ For example, it is also thought that technological changes and the adaptation of companies to changes in the market are a reason for the more frequent use of fixed-term contracts. OECD, *Employment Outlook 2013*, p. 98.

¹⁵⁷ For more, see *Ibid*, p. 98.

¹⁵⁸ Freeman, "Labor market institutions around the world," p. 7.

¹⁵⁹ "Council Directive 1999/70/EC of 28 June 1999 on the Framework Agreement on fixed-term work concluded by ETUC, UNICE and CEEP," *Official Journal of the European Union*, L 175/43, 10 July 1999.

¹⁶⁰ "Council Directive 97/81/EC of 15 December 1997 concerning the Framework Agreement on part-time work concluded by UNICE, CEEP and the ETUC," *Official Journal of the European Union*, L 014/9, 15 December 1997.

¹⁶¹ "Council Directive 98/59/EC of 20 July 1998 on the approximation of the laws of the Member States relating to collective redundancies," *Official Journal of the European Union*, L 225/16, 20 July 1998.

Table 4.1. EPL reforms in European countries according to OECD indicators¹⁶²

Country	Individual and collective dismissals (standard contract)			Individual dismissals (standard contract)			Temporary contracts		
	1993	2003	2013	1993	2003	2013	1993	2003	2013
Austria	2,75	2,37	2,37	2,75	2,37	2,37	1,31	1,31	1,31
Belgium	1,85	1,89	1,89	1,85	1,89	1,89	4,63	2,38	2,38
The Czech Republic	3,31	3,31	2,92	3,31	3,31	2,92	0,50	0,50	1,44
Denmark	2,18	2,13	2,20	2,18	2,13	2,20	1,38	1,38	1,38
Estonia	..	..	1,81	..	..	1,81	..	..	3,00
Finland	2,45	2,17	2,17	2,45	2,17	2,17	1,25	1,56	1,56
France	2,34	2,47	2,38	2,34	2,47	2,38	3,63	3,63	3,63
Germany	2,58	2,68	2,68	2,58	2,68	2,68	3,25	1,50	1,13
Greece	2,80	2,80	2,12	2,80	2,80	2,12	4,75	4,75	2,25
Hungary	2,00	2,00	1,59	2,00	2,00	1,59	0,63	0,63	1,25
Iceland	..	..	1,73	..	..	1,73	..	..	0,63
Ireland	1,44	1,44	1,40	1,44	1,44	1,40	0,25	0,25	0,63
Italy	2,76	2,76	2,68	2,76	2,76	2,68	4,75	2,00	2,00
Latvia	..	..	2,69	..	..	2,69	..	..	0,88
Luxembourg	..	..	2,25	..	..	2,25	..	..	3,75
The Netherlands	3,07	2,88	2,82	3,07	2,88	2,82	1,38	0,94	0,94
Norway	2,33	2,33	2,33	2,33	2,33	2,33	3,13	2,75	3,00
Poland	2,23	2,23	2,23	2,23	2,23	2,23	0,75	0,25	1,75
Portugal	4,58	4,58	3,18	4,58	4,58	3,18	3,38	2,81	1,81
Slovakia	2,47	2,31	1,84	2,47	2,31	1,84	1,38	1,38	1,75
Slovenia	..	..	2,60	..	..	2,60	..	..	1,81
Spain	3,55	2,36	2,05	3,55	2,36	2,05	3,75	3,25	2,56
Sweden	2,80	2,61	2,61	2,80	2,61	2,61	2,77	1,44	0,81
Switzerland	1,60	1,60	1,60	1,60	1,60	1,60	1,13	1,13	1,13
United Kingdom	1,10	1,26	1,10	1,10	1,26	1,10	0,25	0,38	0,38
Average	2,51	2,41	2,21	2,51	2,41	2,21	2,21	1,71	1,73

Source: OECD, 2015.¹⁶³

¹⁶² The indicators contain 21 sub-components that quantify costs and procedures for collective and individual dismissals, fixed-term employment or temporary-work agency employment. The indicators are mostly based on laws, but also take into account collective agreements, and to an extent, also case-law. OECD, *Employment Outlook* 2013, p. 75. For more on the methodology used by the OECD, see the website: <http://www.oecd.org/employment/emp/oecdindicatorsofemploymentprotection.htm> (accessed on 17 December 2015).

¹⁶³ Data retrieved on 28 July, 2015 from the OECD Stats website: https://stats.oecd.org/Index.aspx?DataSetCode=EPL_CD (last accessed on 17 December, 2015). Indicators on additional restrictions on collective dismissal were not used because comparative data prior to 2004 is not available.

In the context of regulatory trends within the EU, there has been a clear tendency to reduce the rigidity of employment protection legislation in the past ten years. Continuous legislative reforms also preceded the financial crisis: between 2003 and 2008, a quarter of OECD countries made conditions for individual and collective dismissals more flexible; however, the focus was not on fixed-term contracts, as in the 1990s.¹⁶⁴ According to the OECD, between 2008 and 2013, or during and immediately after the financial crisis, more than a third of OECD countries relaxed their rules. This was done by some countries with hitherto very strict legislation, such as Portugal, Italy and Greece,¹⁶⁵ which is not surprising, given the role of the European Commission and the IMF in promoting austerity measures due to the large public debt in these countries.

Since the beginning of the crisis, reforms in many countries most often curtailed the possibility for reinstatement following unfair dismissal¹⁶⁶ and extended probationary periods,¹⁶⁷ which are generally considered aspects of employment protection with the greatest influence on overall labor force flows, and especially on transitioning between jobs.¹⁶⁸ In addition, the reasons for justified dismissal have been broadened, severance pay and notice periods have been reduced, and legal remedies for unfair dismissal have been restricted. The flexibility trend is particularly pronounced in Central and Southeast Europe where, during the crisis, in contrast to the majority of other European countries, flexibility was increased for both permanent and temporary workers.¹⁶⁹ On the other hand, in many countries, conditions for temporary-work agency employment have become more stringent, largely as a result of approximation of national legislation with the EU Directive in this realm.

For decades, labor market dualization as a result of partial flexibilization has presented a problem for many European countries. The crisis undermined the job stability of temporary workers even further: companies that hired workers during the crisis mostly did so on temporary contracts due to high uncertainty of demand, while dismissals during the crisis disproportionately affected workers on non-standard contracts, especially youth.¹⁷⁰ According to the OECD, the fact that most countries did not make temporary employment even more flexible during the crisis suggests that decision-makers have become more aware of the problem of labor market duality.¹⁷¹

¹⁶⁴ OECD, *Employment Outlook 2013*, p. 97.

¹⁶⁵ *Ibid.*, pp. 93, 106 and 107.

¹⁶⁶ *Ibid.*, p. 82.

¹⁶⁷ Extending trial periods is another measure that is easy to implement. *Ibid.*

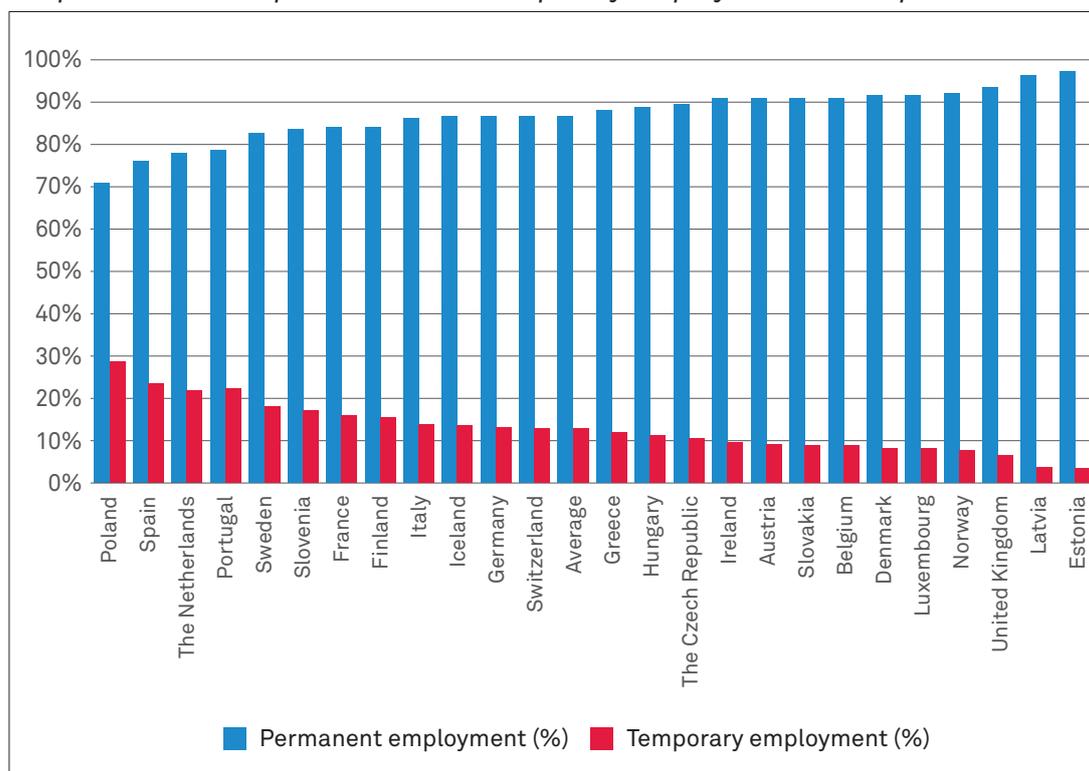
¹⁶⁸ OECD, *Employment Outlook 2013*, p. 96.

¹⁶⁹ Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, p. 11.

¹⁷⁰ Cazes and Tonin (2010) in: Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, p. 15.

¹⁷¹ OECD, *Employment Outlook 2013*, p. 67.

Graph 4.1. Share of permanent and temporary employment in European countries



Source: OECD, 2015.¹⁷²

The most frequently articulated solution to the problem of labor market duality is to make permanent employment contracts flexible in order to “democratize” the (un)employment experience,¹⁷³ which is in line with the current EU reform trends.¹⁷⁴ The other option is a convergence of dismissal costs by applying a single permanent contract,¹⁷⁵ whereby employee protection would increase proportionally with seniority, which would require complex, complementary reforms.¹⁷⁶ For example, by introducing a single contract, individual service contracts that are not subject to employment protection legislation may be abused, which would also have to be regulated. Given that dualism is also affected by institutional obstacles (e.g. lack of efficiency of court procedures, strategic use of temporary contracts, etc.) and structural obstacles (e.g. reduced

¹⁷² Total labor force (15–65+), all workers, non-independent employment; data retrieved on 28 July, 2015 from OECD Stats: http://stats.oecd.org/Index.aspx?DataSetCode=EPL_OV (accessed on 17 December, 2015).

¹⁷³ Esping-Andersen and Regini, “Introduction,” p. 3.

¹⁷⁴ OECD, Employment Outlook 2013, p. 97.

¹⁷⁵ Ibid, p. 70.

¹⁷⁶ Convergence has so far been achieved to a certain degree by Ireland, New Zealand and the United Kingdom, although they have still retained temporary contracts to afford companies a measure of flexibility, especially for temporary jobs. These countries have low levels of employment protection and limited judicial review of terminations. OECD, Employment Outlook 2014, p. 144.

productivity and competitiveness of the economies of South Europe), Cazes et al. believe that broader reforms are necessary to improve transitioning between temporary and permanent employment.¹⁷⁷

4.1.3. Employment Protection in Bosnia and Herzegovina

Labor legislation pertaining to employment protection (EPL) in Bosnia and Herzegovina comprises labor laws,¹⁷⁸ collective agreements and case law pertaining to labor relations. The labor laws adopted in 1999 in FBiH and in 2000 in the RS introduced changes compared to previous legislation in this area inherited from the former Yugoslavia, and made working conditions, to a certain extent, more flexible.¹⁷⁹ Still, when it comes to employment protection in general, BiH is characterized by inertness and long-term maintenance of the *status quo*, which can be explained, among other things, by efforts to mitigate the consequences of the recession caused by wartime destruction and the transition from a planned to a market economy¹⁸⁰. However, as part of current reform efforts, described above, a new Labor Law was adopted in FBiH in July 2015, and activities are under way to change labor legislation in the RS in an effort to address the numerous problems of the labor market. In further text, this section provides an overview of the most significant aspects and reform efforts related to employment protection legislation in BiH.

As a general rule, in both entities and the Brčko District, termination of employment is possible when it is justified by economic, technical or organizational reasons, or when the worker, given his/her professional and working capabilities, is not able to perform the tasks required under the employment contract, but provided that the employer is unable to employ or train the worker for another position. In addition, the employer may dismiss a worker for a major offence or violation of contract.¹⁸¹

In the event of unlawful dismissal, the court may order the employer to reinstate the worker either in the same position occupied prior to dismissal or in another position corresponding to the worker's qualifications and capabilities, as

¹⁷⁷ Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, p. 24.

¹⁷⁸ "Zakon o radu Republike Srpske" [Labor Law of Republika Srpska], *Official Gazette of Republika Srpska* 38/00, 40/00, 47/02, 38/03, 66/03, "Zakon o radu Federacije BiH" [Labor Law of the Federation of BiH], *Official Gazette of the Federation of BiH* 62/15, "Zakon o radu Brčko distrikta" [Labor Law of the Brčko District], *Official Gazette of the Brčko District*, 19/06, 19/07, 25/08, 20/13, 31/14, 1/15. There is also a special group of laws pertaining to civil service employees.

¹⁷⁹ For example, see CEST FBiH and CEST RS, "Modul 2: Radno zakonodavstvo Bosne i Hercegovine, radni odnosi u praksi" [Module 2: Labor Legislation of Bosnia and Herzegovina, Labor Relations in Practice] (2007), p. 13.

¹⁸⁰ International Labor Organisation and the Council of Europe, *Pregled politika zapošljavanja: Bosna i Hercegovina* [Employment Policy Review: Bosnia and Herzegovina] (Council of Europe, 2009), p. 31.

¹⁸¹ Labor Law of FBiH, Articles 96 and 97; Labor Law of Republika Srpska, Article 126; Labor Law of BD, Articles 73 and 74.

well as to pay compensation for withheld salaries and other income the worker would have received in the period from the termination of the employment contract until the enforcement of the judgement. In addition, legislation in FBiH and BD also foresees the possibility of paying compensation of salary, damages, severance pay and other compensations in line with valid regulations, rulebooks and the contract, without a continuation of the employment relationship between the worker and the employer.¹⁸²

The employer is obliged to inform the worker of dismissal in writing and provide justification.¹⁸³ The minimum notice period when the employer is terminating the employment contract is not uniform throughout the territory of BiH. Thus, the minimum notice period can be no less than 14 days in FBiH and BD, and no less than 30 days in the RS, and runs from the date of delivery of dismissal to the employee. If the worker has committed a major offence or breached the terms of the employment contract, the employer is not obliged to uphold the stipulated notice period when terminating the employment contract.¹⁸⁴

Although for standard individual dismissals, the employer is not obliged to consult other actors (unions, the competent ministry, etc.), collective dismissals resulting from economic, technical or organizational reasons require that the employer consult the workers' council and/or representative union. In FBiH, the obligation to consult applies to employers of over 30 workers, who plan to dismiss at least five workers over the subsequent three months. In the RS and BD, it applies to employers of over 15 workers planning to dismiss at least 10% of the total number of employees, but not less than five workers in the RS, or at least 20% of the employees in BD, in the period of up to three (RS) or more than three months (BD). Consultations are based on a written act in which the employer justifies the reasons for the dismissals, the number and category of workers to be dismissed, proposes measures to potentially avoid some or all dismissals, and finally, measures that would facilitate the employment of dismissed workers elsewhere. The employer is obliged to start the consultation process at least 30 days prior to issuing notices of dismissal to workers. Finally, if the employer plans to hire workers with the same profile and level of qualifications within one year from the date of termination of employment of the dismissed workers, the employer shall be obliged to offer employment to the dismissed workers first. Nevertheless, employers are not obliged, as is the case in some countries, to negotiate with unions on collective dismissal.¹⁸⁵

¹⁸² Labor Law of FBiH, Article 106; Labor Law of Republika Srpska, Article 130; Labor Law of BD, Article 81.

¹⁸³ Labor Law of FBiH, Article 104; Labor Law of Republika Srpska, Article 127; Labor Law of BD, Article 79.

¹⁸⁴ Labor Law of FBiH, Articles 97 and 105; Labor Law of Republika Srpska, Article 135; Labor Law of BD, Articles 74 and 80.

¹⁸⁵ Labor Law of FBiH, Articles 109 and 110; Labor Law of Republika Srpska, Articles 138, 139, and 140; Labor Law of BD, Articles 83 and 84.

An employer may not dismiss a union representative during his or her mandate or for a certain period (12 months in the RS, 6 in FBiH, and 3 in BD) following the expiration of his or her mandate, without consultation or approval of dismissal by the relevant authority - the ministry in charge of labor affairs in FBiH and RS and the union in BD.¹⁸⁶

Workers whose permanent employment contracts are terminated following two successive years in service are entitled to severance pay (except for cases when termination results from breach of contract). The amount of severance pay and other terms are determined by the collective agreement, employment rulebook, employment contract, and in the case of BD, a written agreement between the employer and the employee. Still, the amount of severance pay may not be less than one third of the average monthly salary paid to the worker in the three months preceding dismissal for each year of employment, while in FBiH it also cannot be more than six average monthly salaries paid to the worker in the three months preceding dismissal.¹⁸⁷

Concerning standard fixed-term employment contracts, in FBiH, these may be signed with a single employer, irrespective of whether this entails one or more consecutive contracts (and there is no limitation to the number of consecutive contracts that may be signed), for a period of three years' maximum, while in the RS and BD, they may be signed for up to two years maximum. In addition, an employment contract extended after this period is considered permanent, except when there were suspensions of employment between contracts (suspensions do not include leave and temporary incapacitation for work as stipulated by law, employer-approved leave, etc. or any periods between two contracts lasting up to 60 days in FBiH, or up to 15 days in BD). In the RS, the regulations are somewhat stricter and foresee permanent employment if the worker is employed by the same employer multiple times based on a fixed-term contract and thereby accumulates 24 months of employment within three past years. When it comes to conditions under which it is possible to sign a fixed-term employment contract, there are no restrictions defined by law in FBiH, while in the RS and BD fixed-term contracts are allowed in exceptional cases: for jobs up to 6 months in duration (RS), seasonal work (BD), project-based work and jobs whose duration is predetermined by the nature and type of work, temporary replacement of an absent employee, and temporary expansion of the company's activities.¹⁸⁸ There are currently no temporary work agencies in BiH, and no regulations or mechanisms for employment protection in this domain.

¹⁸⁶ Labor Law of FBiH, Article 103; Labor Law of Republika Srpska, Article 131; Labor Law of BD, Article 78.

¹⁸⁷ Labor Law of FBiH, Article 111; Labor Law of Republika Srpska, Article 141; Labor Law of BD, Article 85.

¹⁸⁸ Labor Law of FBiH, Articles 22 and 23; Labor Law of Republika Srpska, Articles 16, 17, and 18; Labor Law of BD, Articles 12 and 13.

Labor legislation in BiH is assessed as especially rigid due to high levels of employment protection,¹⁸⁹ and in the past few years, international financial institutions and the European Union have proposed increasing the flexibility of employment in order to encourage the creation of new jobs and economic growth. Thus, for example, the Compact for Growth and Jobs proposes greater flexibility of the labor market in order to reduce “disincentives for hiring,” and for employers to have a “measure of flexibility before they will employ an expensive workforce,” and given that, as the document points out, high costs of the dismissal process, combined with administrative barriers, discourage employers from employing (new) workers.¹⁹⁰ In practice, changes to labor legislation aim to “make it easier for employers to adjust staffing levels when circumstances change and shift workers from the grey economy to the formal sector.”¹⁹¹

According to estimates of employment protection indicators in the segment of individual and collective dismissals for permanent employment in BiH, published by the OECD in January 2015,¹⁹² this set of indicators was 2.52, while, for the sake of comparison, the average in OECD countries for 2013 was 2.04¹⁹³ (see Graph 4.2).¹⁹⁴ However, the EPL for BiH is not significantly greater than the average of the 25 countries that belong to Europe (2.21), or the group of new EU member states (2.24)¹⁹⁵ covered by the OECD index. On the other hand, previous assessments of indicators for temporary contracts in BiH (2.9) showed that EPL in this segment was more rigid than the EU15 average¹⁹⁶ (2.0). Also, the indicator for collective dismissals (3.3) was somewhat lower than the EU15 average (3.4).¹⁹⁷ It is worth noting that these indicator assessments pertain only to the labor laws of the entities. In other words, the application of the law in practice was not taken into account, even though it is considered extremely important in countries with a considerable

¹⁸⁹ Kovtun et al, “Boosting Job Growth in the Western Balkans.”

¹⁹⁰ EU Delegation to BiH, Compact for Growth and Jobs in BiH, p. 6.

¹⁹¹ IMF, BiH: Second Review Under the Stand-By Arrangement and Requests for Waivers of Applicability and Modification of Performance Criteria – Staff Report; Press Release; and Statement by the Executive Director (IMF, 2013), p. 15.

¹⁹² See OECD, “Bosnia-Herzegovina,” OECD Indicators of Employment Protection (2015).

¹⁹³ OECD Stats, “Strictness of employment protection – individual and collective dismissals (regular contracts).”

¹⁹⁴ The OECD did not measure EPL rigidity indicators for temporary work. Graph 10 also applies to countries with data available for 2013, but which are not necessarily OECD members. The OECD average pertains only to OECD member states.

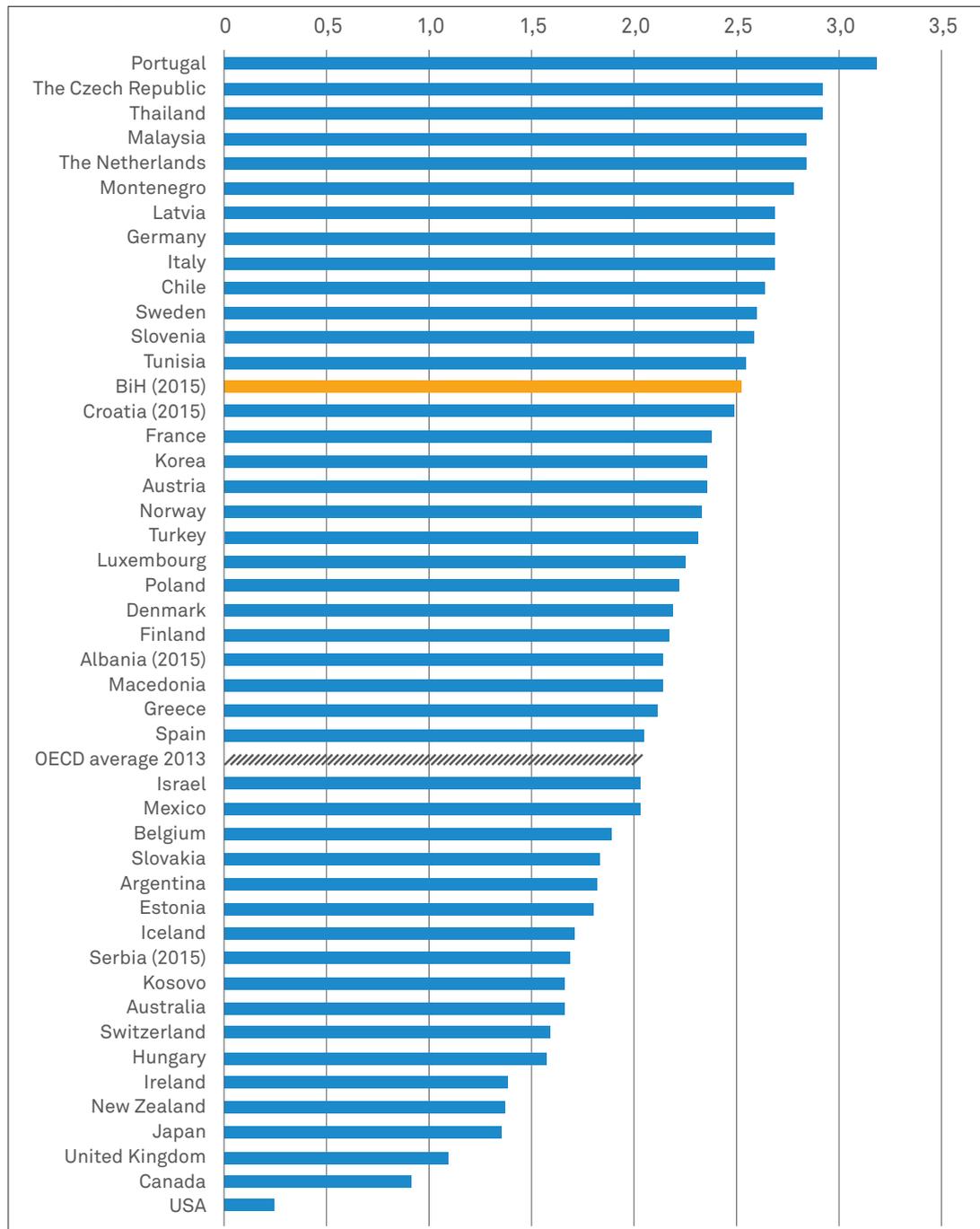
¹⁹⁵ The Czech Republic, Slovakia, Poland, Slovenia, Hungary, Estonia, and Latvia (EPL for 2013).

¹⁹⁶ Refers to the number of EU member states prior to the 2004 enlargement: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, The Netherlands, Portugal, Spain, Sweden, United Kingdom.

¹⁹⁷ In reference to the EU15 average for 2003. Assessment of EPL indicators for BiH pertains to 2007. ILO, *Delivering decent work in Europe and Central Asia (I/II)* (Geneva: ILO, 2009), pp. 53–55. It should be noted that indicators for employment protection legislation measured by the ILO in 2007 and the OECD indicators from 2015 are not comparable because the OECD changed its methodology in 2008.

grey economy, and neither was case law related to employment. Differences in employment protection legislation for employees in the public as opposed to those in the private sector were also left out. The application of employment protection legislation in practice could yield a different picture of potential rigidities.

Graph 4.2. EPL in OECD and Western Balkan countries (2013 and 2015)



Sources: OECD Stats¹⁹⁸

¹⁹⁸ OECD Stats, "Strictness of employment protection – individual and collective dismissals (regular contracts)."

The adoption of the new Labor Law (LL) of FBiH in mid-2015 meant certain steps towards making labor legislation more flexible in this entity and fulfilling the reform objectives set out by the Reform Agenda.¹⁹⁹ Although opinions are divided among social partners and experts on whether the new LL in FBiH brings substantial or “cosmetic” changes compared to the previous law, it is certain that it has made employment more flexible in all dimensions:

- *external*: extending the maximum duration of fixed-term contracts from 2 to 3 years; simplifying dismissing workers with changed abilities also after temporary incapacitation, etc.
- *temporal*: introducing the institute of availability for work; authorizing the employer to determine annual leave schedules, etc.
- *wage*: changing the structure of salaries, whereby the salary for work performed and time spent working consists of the main salary, part of the salary for work performance and increased salary; reducing the salaries for interns from 80% to 70% of the salary assigned to the position for which the intern is training; reducing severance pay; negotiating a new collective agreement that will define minimum wages, compensations that are not counted as salary and other aspects relevant to determining the price of work, etc.
- *functional*: flexibilization of the workplace; enabling one-sided decisions on the allocation of workers to other positions in emergency situations, etc.

It should be noted that the current reform documents stress increasing the flexibility of working conditions on the premise that entity labor laws negatively affect unemployment, and that changing them will encourage the creation of new jobs. Still, they do not refer to research in this domain, which has seriously questioned the assumption that unemployment results from rigid employment protection. Even if we disregard international comparative analyses in this domain, it is worth noting that even analyses of employment protection legislation in countries of the Western Balkans, though rare, have not generally shown a

¹⁹⁹ At the same time, we should not lose sight of the fact that the new Labor Law in FBiH also brings certain improvements in terms of the position of workers, primarily by reducing the possibilities for abuse of certain provisions of the Law.

significant influence of EPL on employment and unemployment.²⁰⁰ Moreover, the experience of various European countries showing that positive outcomes in the labor market cannot be unequivocally attributed to deregulation, but are the result of a number of other factors, such as the interactions between various labor market institutions and the general economic situation, are not considered. Current reform proposals do not include assessments on whether and to what extent the current regulatory framework of employment protection is truly rigid, and to what extent poor labor market performance may be attributed to labor legislation as opposed to other important factors, such as the reduced scope of economic activity and low demand.

It is also concerning that the abovementioned reform proposals do not sufficiently examine the potential risk posed by greater flexibilization of temporary as opposed to permanent employment contracts, which may contribute to segmentation in the labor market. Although there is the possibility that a certain group of the unemployed, such as youth, women, low-skilled workers and others, could find employment easier due to partial flexibilization, it is also important to take into account the potential negative effects: for example, in the long term, these groups may be forced to accept fixed-term contracts, frequently changing jobs and enjoying lower job security and quality. In the recently adopted Labor Law in FBiH, flexibility of working conditions for fixed-term contracts pertains to the duration of such arrangements – the maximum period of duration of such contracts has been extended from 24 to 36 months.²⁰¹

There is also the question of whether or not the current proposals truly address any rigidities of employment protection legislation in practice. Although there are no reliable or comprehensive statistical data in the realm of judicial protection, various sources usually indicate long and inefficient employment disputes in courts in BiH, burdensome for both the employee and the employer, and which should be taken into account in the interest of effective application of legislation. The reforms, for example, do not mention the need to improve judicial and extra-judicial mechanisms for resolving employment disputes.

²⁰⁰ See, for example, Micevska (2004). Analyzing countries of East and Southeast Europe, Micevska nevertheless found that stricter employment protection for temporary employment increases the unemployment rate for women and youth, and decreases labor force participation. On the other hand, Nikolov (2005) attributed similar results in Macedonia to the lack of adequate labor force education, inefficient privatization, weak institutions and unfavorable investment conditions, rather than stringent employment protection. After analyzing various labor market institutions, Arandarenko (2004) concludes that there is no solid evidence for the assumption that more flexible labor regimes lead to better economic results. Discussed in: DG for Economic and Financial Affairs and Vienna Institute for International Economic Studies, *Adjustment capacity of labour markets of the Western Balkan countries*, p. 27. The analysis of the European Commission and the Vienna Institute for International Economic Studies suggests an impact of stricter regulation of temporary employment, in increasing unemployment of women, but decreasing unemployment of men; and an impact of stricter regulation of collective dismissals, in increasing unemployment of men, but decreasing unemployment of women. *Ibid*, p. 65.

²⁰¹ Labor Law of FBiH, Article 22.

In any case, it seems that the current reform proposals do not sufficiently account for discussions of EPL impact on labor market performance in this realm, although they have changed significantly since the time when the previously mentioned OECD Jobs Study, which provided a framework for the paradigm of labor market deregulation. Thus, the discourse of “flexibility at any price” has in the meantime also been mitigated following the recognition of the importance of job security and quality.

4.2. Price of Labor, Taxes and Contributions

4.2.1. Definitions, Key Discussions and European Trends

The price of labor is determined by labor taxation policies, minimum wage policies and policies aimed at making work pay (i.e. in-work benefits):

- The tax wedge is the difference between total cost of labor and the “take-home” wage received by employees, and is usually represented in relative terms as the ratio between the sum of income taxes and social security contributions (e.g. pension insurance, healthcare, unemployment insurance) paid by the employee and/or employer, on the one side, and the total costs of labor, which, apart from taxes and contributions, also include the net wage, on the other.²⁰²
- Minimum wages are the lowest salaries set by law or collective agreement that may be paid to all or a certain category of workers in the country or in a specific sector.
- In-work benefits, paid in the case of low income, are a means of activation, or an incentive to inactive and unemployed persons who, due to low potential earnings, have little motivation to accept a job, or an incentive to employed workers to keep their jobs. They are paid as monetary benefits or a tax credit or deduction.

In economic theory, it is expected that increased labor costs will reduce demand for labor. According to some studies, any increase in the price of labor that is not accompanied by an adequate increase in productivity, results in the increase of unit labor costs, which ultimately reduces competitiveness and results in decreased demand for workers, or in extreme cases, to lay-offs.²⁰³ It is, therefore, thought that a certain degree of flexibility in determining salary levels contributes to better mediation of market fluctuations and the retention of existing jobs, or ultimately enables greater demand in the labor market, when needed.

²⁰² OECD, *Taxing wages 2013–2014* (Paris: OECD, 2015), p. 17.

²⁰³ See in Kovtun et al, “Boosting Job Growth in the Western Balkans.”

According to Arandarenko and Vukojević, a high tax wedge discourages employment in the formal sector by increasing labor costs for the employer, which has a detrimental effect on labor demand and reduces “take-home” wages, which may in turn limit the supply of labor. In Western Balkan labor markets, with their high unemployment rates and surplus labor force, the effect of taxes on demand is more relevant than an effect on supply.²⁰⁴ Also, the high tax wedge on the lowest salaries has most probably contributed to widespread informal employment and high unemployment.²⁰⁵

There is also an assumption that a significant increase in minimum wages can lead to lay-offs, informal employment or reduced working hours for some employees. Nevertheless, influential studies in this domain have not unequivocally shown any significant impact of moderate increases of the minimum wage on unemployment,²⁰⁶ and there is even some evidence that moderate increases of minimum wages can lead to an increase in workers’ productivity. Still, the employment of certain groups, such as youth, may be undermined if minimum wages are high and the labor market is weak (e.g. after a period of crisis).²⁰⁷

On the other hand, empirical research has also indicated positive effects of introducing certain types of in-work benefits (especially on the participation of certain categories of the labor force, such as women, in the labor market) and their positive redistributive effects (decreased inequality and poverty among the employed).²⁰⁸

Graph 4.3 shows the tax wedge for a single person without children at 100% of average earnings in European countries, members of the OECD, for 2014. It is evident that the average tax wedge in these European countries is considerably higher (40.67%) compared to the average in OECD countries (35.95%).

²⁰⁴ Arandarenko and Vukojević, *Labor Costs and Labor Taxes in the Western Balkans*, p. 55.

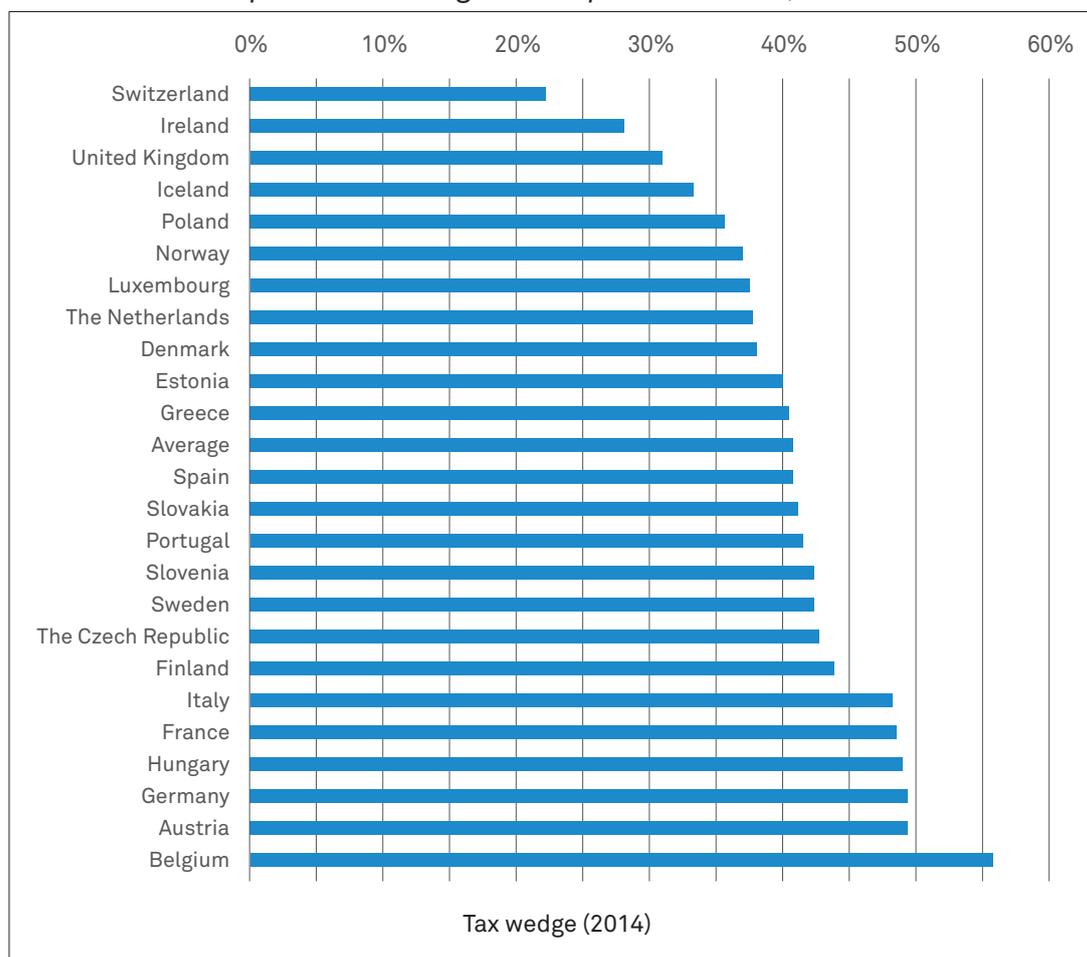
²⁰⁵ *Ibid.*, p. 58.

²⁰⁶ According to a significant study by Card and Krueger, in the late 1980s and early 1990s, the increase of minimum wages in some US states, as well as the increase of the federal minimum wage, did not have any effect (or had positive effects) on employment. Freeman, “Single Peaked vs. Diversified Capitalism,” p. 21.

²⁰⁷ OECD, *Taxing wages 2013–2014*, p. 9.

²⁰⁸ Herwig Immervoll and Mark Pearson, “A Good Time for Making Work Pay? Taking Stock of In-Work Benefits and Related Measures across the OECD,” Working Paper No. 81 (OECD Publishing, 2009), pp. 6, 28–35.

Graph 4.3. Tax wedge in European countries, OECD²⁰⁹



Source: OECD, 2014²¹⁰

There are significant differences among countries in terms of the structure of the tax wedge, especially with regard to personal income tax. For example, among European countries, the highest level of income tax is found in Denmark (35.6%), and the lowest in Poland (6%).²¹¹ The percentage of labor costs allocated to social security benefits also varies considerably: from, 2.8% in Denmark, for instance, to 37.9% in France.²¹² In most countries, there are also significant differences in the amount of income tax paid by individuals as opposed to families: for example, a family with two children and one employed member with average wage earnings pays significantly less tax than a single employed individual with average wage earnings. In some countries, such as the Czech Republic and Slovakia, due to tax

²⁰⁹ Average tax wedge, a single individual without children, 100% of average wage level earnings.

²¹⁰ OECD, Taxing wages 2013–2014, p. 8.

²¹¹ Ibid, p. 21.

²¹² Ibid.

credits, such families have negative income tax.²¹³ In four European countries (the Czech Republic, Slovakia, Germany and the UK), single parents with two children who make 67% of the average wage also have a negative tax burden, while in two countries (Poland and Slovenia), such families do not pay income tax.²¹⁴

Another important aspect of the tax system is the level of progressivity, i.e. the rate at which the tax burden increases with income. If we look at the tax burden for an individual with average wage earnings and an individual with earnings at the 167% wage level, those with lower pay have a lower tax burden in all European countries, apart from Hungary, where there is a flat tax rate on income. When social security contributions are added, progressivity is reduced, as are proportional savings that are enjoyed by families.²¹⁵

In essence, policies of labor taxation, minimum wages and making work pay are important complementary instruments for resolving labor market issues. States define minimum wages by law to ensure basic protection for workers, usually in combination with collective agreements that define the minimum wage for a specific sector. In the EU, 22 out of 28 member states have defined minimum wages. In order to provide incentives for employment, many states have defined a lower minimum wage for youth, apprentices or those entering the labor market for the first time (e.g. the Netherlands, the United Kingdom).²¹⁶ According to the OECD, in the past few years, a number of countries have increased minimum wages in the context of high unemployment and stagnating or decreasing real wages, as well as labor market segmentation and wage inequality. The effectiveness of minimum wage policies, as a means of support for low-income workers and families, also depends on the tax wedge: as noted by the OECD, even when it comes to the lowest income, taxes and social security contributions can significantly reduce the worker's "take-home" pay and increase the cost of employing minimum wage workers.²¹⁷

This is why some countries have opted for specific measures such as tax benefits for employers taking on minimum wage workers, as well as for the workers themselves (e.g. paying lower social contributions or personal income tax), or introduced progressive tax rates to reduce the tax burden on those with the lowest income. The combination of in-work benefits or tax credits with minimum wages is regarded as an efficient solution also because such benefits can be targeted, and because employers will not be able to abuse such benefits, as they could reduce wages for the amount of in-work benefits.²¹⁸ In the UK, for example, benefits are means-tested and are a combination of cash benefits

²¹³ The tax burden is -4.4% in the Czech Republic, and -2.5% in Slovakia. *Ibid.*, p. 45.

²¹⁴ *Ibid.*, p. 45.

²¹⁵ *Ibid.*, pp. 45–46.

²¹⁶ OECD, *Employment Outlook 2014*, p. 68.

²¹⁷ *Ibid.*, pp. 68-69; 72.

²¹⁸ *Ibid.*, pp. 13-24, 46, 68-69;

and tax credits, and they are reduced as employment income increases in line with the principle of making work pay. Mean-tested benefits have been unified into a unique benefit, which also integrates various family support, and which is reduced or withdrawn as work income increases. The great challenge in this system is collecting continuously updated income information so that benefits are paid to those in need.²¹⁹

In any case, interactions between wages, taxes and benefits require careful coordination to avoid negative effects. The levels of minimum wages, taxes and tax credits need to be carefully determined to achieve the desired effects of a given policy (e.g. reducing the poverty of families or certain categories of workers, etc.). For example, in-work benefits and tax credits narrowly aimed at low-income workers, and that are withdrawn as soon as their wages rise above the minimum, may reduce motivation on the part of workers to advance and accept better paying jobs, and may also lead to abuses in reporting income. On the other hand, benefits that are not as targeted do not carry such consequences, but can be extremely expensive as public policy tools. The application of tax credits or benefits must also be carefully thought out: for instance, determining benefits based on family income usually entails more generous benefits, but may demotivate women to participate in the labor market. On the other hand, such effects can be avoided if benefits are determined based on income of an individual, but are then less generous.

4.2.2. Labor Costs in Bosnia and Herzegovina: Price of Labor and the Burden on Labor

In the years of the economic crisis, real increase in wages continued in Bosnia and Herzegovina despite a parallel increase in unemployment.²²⁰ According to an IMF study on the Western Balkans, this situation could have resulted from existing institutional rigidities, which include high levels of employment protection and an inflexible structures of wage bargaining.²²¹ Thus, most of the abovementioned reform proposals and recommendations related to the labor market insist on more flexibility and redesigning bargaining to determine labor prices, while at the same time, as part of the NERP, an increase in the minimum wage in both entities is foreseen as a measure of security.²²²

Although they have not been explicitly addressed in reform proposals to date, there are different opinions on whether minimum wages in BiH constitute an obstacle to greater employment. According to the IMF study on the Western Balkans, in all economies of the Western Balkans, apart from Montenegro,

²¹⁹ John P. Martin, "Activation and Active Labour Market Policies in OECD Countries: Stylized Facts and Evidence on their Effectiveness," Policy Paper No. 84 (Bonn: IZA, 2014), pp. 25-26.

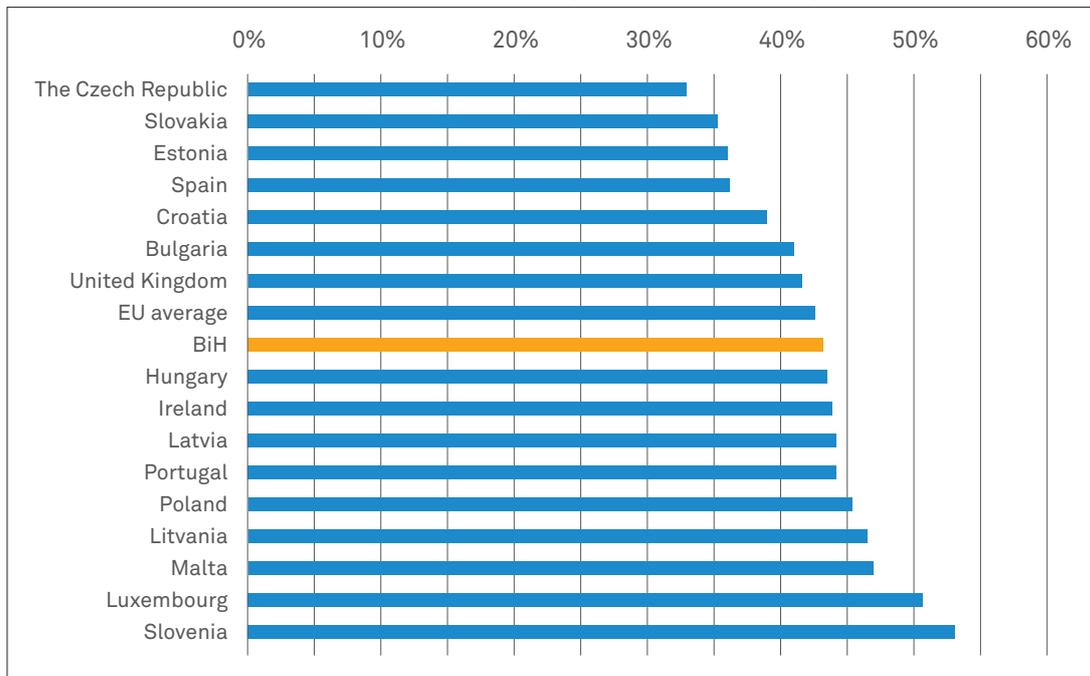
²²⁰ Kovtun et al, "Boosting Job Growth in the Western Balkans," p. 14.

²²¹ Ibid.

²²² Council of Ministers of BiH, National Economic Reform Programme for 2015, pp. 107 and 120.

minimum wages are too high.²²³ Nevertheless, the minimum wage in BiH is about 43% of average gross salary, which is close to the average of EU countries with set minimum wages (Graph 4.4).²²⁴

Graph 4.4. The minimum monthly wage in EU countries with set minimum wages and in BiH, in proportion to average monthly earnings (%), 2014.



Source: Eurostat, 2015; calculations by the authors

O'Higgins analyzed the potential influence of minimum wages on the employment of young people in the informal economy in BiH, using data from the Labor Force Survey from 2006 and comparing the differences in minimum wages between the entities in relation to the incidence of informal employment of young people. He could not confirm the assumption that the minimum wage plays an important role for informal employment of young people. The author points out that the minimum wage in the formal sector generally does not significantly differ than the one in the informal sector. Even though this is descriptive evidence,

²²³ This is in line with the recommendation of Rutkowski (2003), that for countries with high unemployment rates concentrated among young and low-skilled workers, the minimum wage should not exceed more than one third of the average salary. In: Kovtun et al, *Boosting Jobs and Growth in the Western Balkans*, p. 15. On the other hand, according to Arandarenko and Vukojević (2008), the general rule is that minimum wages should be at about 40% of the average salary. Mihail Arandarenko and Vladimir Vukojević, *Labor Costs and Labor Taxes in the Western Balkans* (World Bank, 2008), p. 60.

²²⁴ Non-weighted average for BiH. Authors' calculations are based on the lowest net hourly wage in FBiH defined by collective agreement (1.95 BAM) and the defined monthly net minimum wage of 370 BAM in the RS, calculated with taxes and benefits, and the average gross salary in both entities for 2014. In the RS it is around 44%, and in FBiH around 41% of the average salary. See also Kovtun et al, *Boosting Jobs and Growth in the Western Balkans*, p. 15.

following employment and unemployment trends in relation to minimum wage changes, he concludes that minimum wages do not seem to have a strong detrimental effect on employment in BiH, although they may have some impact on the distribution of employment between the formal and informal sectors.²²⁵

In the context of labor cost, more attention is devoted to the tax wedge in BiH, which, according to international financial institutions, the EU and some experts, is too high compared to the average in new EU member states,²²⁶ which, in view of the local economic context,²²⁷ has a negative effect on labor demand, impeding economic growth and facilitating the expansion of the informal labor market. Most of those we were able to consult during our research agree with these assessments.

According to our calculations,²²⁸ the tax wedge for an individual without children,²²⁹ whose gross salary is at the level of the average annual gross salary for 2014,²³⁰ is 41.7% in FBiH,²³¹ and 38.2% in the RS. In other words, for a worker in FBiH whose gross salary amounts to 1,272.00 BAM, the total labor cost is

²²⁵ For more details, see: Niall O'Higgins, "Bosnia and Herzegovina: Wage trends and policies in response to the financial and economic crisis," *The Impact of the Crisis on Wages in South-East Europe*, eds. Verena Schmidt and Daniel Vaughan-Whitehead (Geneva: ILO, 2011), pp. 58–59, 68–69.

²²⁶ Kovtun et al, "Boosting Job Growth in the Western Balkans," p. 9; and EU Delegation to BiH, Compact for Growth and Jobs in BiH.

²²⁷ See EU Delegation to BiH, Compact for Growth and Jobs in BiH.

²²⁸ Calculations are based on the following laws: "Zakon o doprinosima Federacije BiH" [Law on Contributions of the Federation of BiH], *Official Gazette of the Federation of BiH* 35/98, 54/00, 16/01, 37/01, 1/02, 17/06, and 14/08; "Zakon o doprinosima Republike Srpske" [Law on Contributions of Republika Srpska], *Official Gazette of Republika Srpska* 116/12; "Zakon o porezu na dohodak Federacije BiH" [Law on Income Tax of the Federation of BiH], *Official Gazette of the Federation of BiH* 10/08, 9/10, 44/11, 7/13, and 65/13; "Zakon o porezu na dohodak" [Law on Income Tax], *Official Gazette of Republika Srpska* 91/06, 128/06, 120/08, 71/10, 1/11, 107/13.

²²⁹ The laws on income tax foresee personal deductions for dependant family members.

²³⁰ Data on salaries from: Federal Institute for Statistics, "Statistički bilten br. 218: Zaposlenost, nezaposlenost i plaće u Federaciji Bosne i Hercegovine 2014" [Statistical Bulletin No. 218: Employment, Unemployment and Wages in the Federation of Bosnia and Herzegovina 2014] (Sarajevo: Federal Institute for Statistics, 2015), p. 11; Republika Srpska Institute for Statistics, "Statistički bilten br. 7: Plate, zaposlenost i nezaposlenost" [Statistical Bulletin No. 7: Wages, Employment and Unemployment] (Banja Luka: Republika Srpska Institute for Statistics, 2015), p. 9.

²³¹ The calculation for FBiH is shown with and without non-taxable work-based benefits such as meal and transport allowances, which have "due to relatively high rates of contributions and taxes [...] to a considerable extent taken on the role of salaries." Bonuses were not included in the calculation because we believe they have minimal effect on the tax wedge given that they are usually paid only once in a calendar year and are at the discretion of the employer. Still, it should be noted that not all employees receive bonuses, meal and transport allowances, and that their amount is not directly related to the level of gross salary, and that they ultimately do not constitute a formal part of the salary. Data on non-taxable benefits and quotations sourced from: Federal Institute for Development Programming (FIDP), *Analiza modela oporezivanja svih naknada po osnovu rada u Federaciji Bosne i Hercegovine* [Analysis of Taxation Model for All Work-Based Benefits in the Federation of Bosnia and Herzegovina] (Sarajevo: Federal Institute for Development Programming, 2015), p. 8.

1,405.56 BAM,²³² while the “take-home” earnings are 819.91 BAM. In the RS, a worker whose gross salary amounts to 1,334.00 BAM – which is also the total cost of labor – will receive “take-home” earnings in the amount of 824.40 BAM (Table 3). As for the structure of the tax wedge, income tax in both entities is 10%, while most of the labor burden consists of various social contributions.

Table 4.2. Tax wedge in BiH, individual, average annual gross salary, 2014

		With untaxed allowances for meal and transport ²³³	Without untaxed allowances for meal and transport
FBiH	67% of average salary	31.67%	40.60%
	100% of average salary (1,272 BAM)	35.04%	41.70%
	167% of average salary	38.19%	42.50%
RS	67% of average salary	-	39.70%
	100% of average salary (1,334 BAM)	-	39.70%
	167% of average salary	-	39.70%

Source: calculation by the authors²³⁴

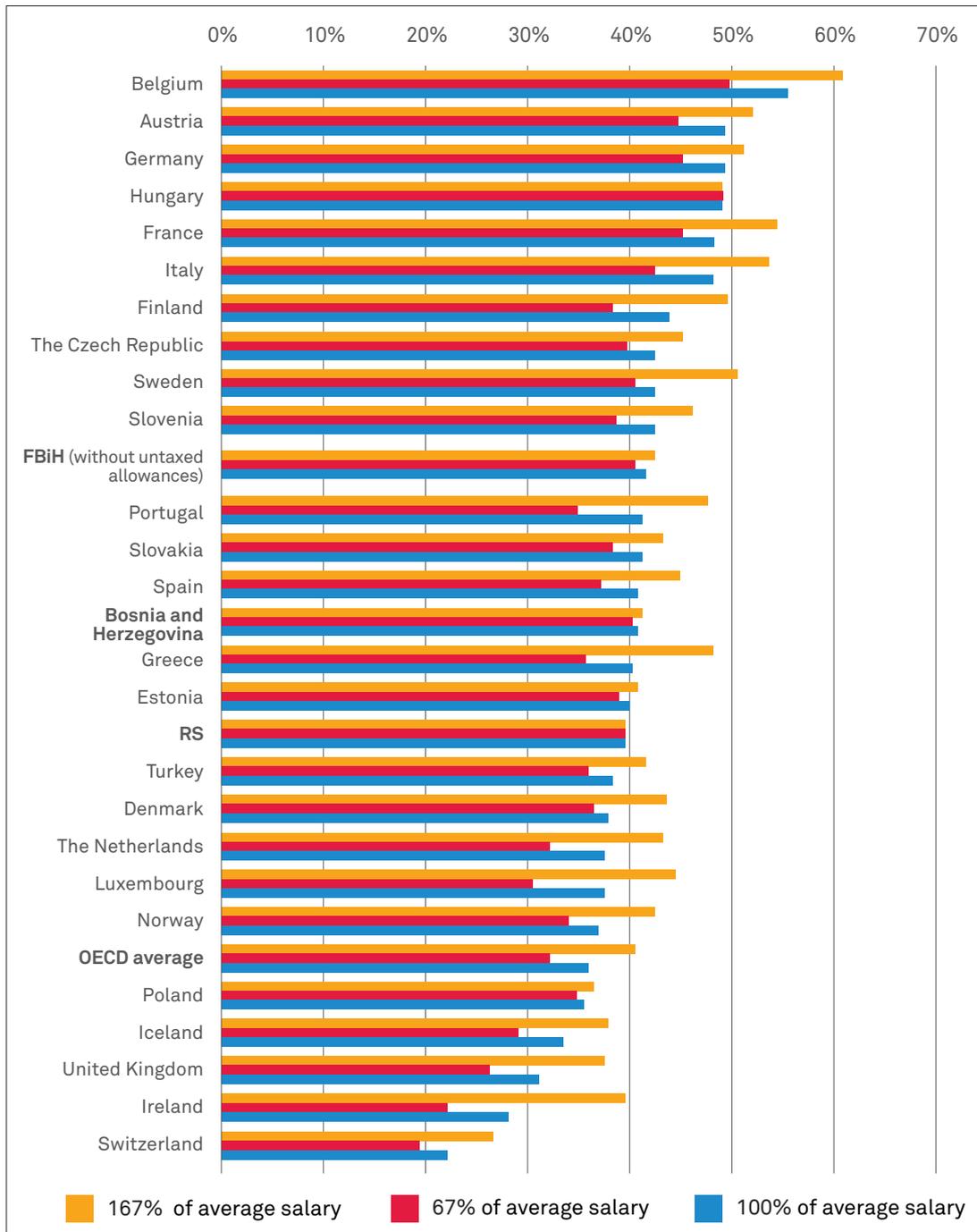
The tax wedge in BiH for a worker with average pay is higher than the OECD average of 36% (see Graph 4.5), if we take into account the average without meal and transport allowances in FBiH. Still, it is close to the 40.67% average in European countries that are OECD members and is lower than the 41.83% average of new EU member states, also members of the OECD (the Czech Republic, Estonia, Hungary, Poland, Slovakia and Slovenia).

²³² Due to the specific calculation of salaries and contributions in FBiH, where apart from contributions from the gross salary (so-called *contributions borne by the employee*), contributions are also paid on top of (gross) salary (so-called *contributions borne by the employer*), the total real labor costs are higher in relation to the nominal gross salary. These total labor costs (gross salary + contributions) were used to calculate the tax wedge, given that in FBiH the gross salary – which is the basis for calculating the net salary – does not include all the actual labor costs.

²³³ In the RS, meal and transport allowances are taxable and are part of the gross basis for calculating contributions from salaries. FDPI, *Analysis of Taxation Model for All Work-Based Benefits*, p. 5.

²³⁴ Average amounts for 2014 were used to calculate transport and meal allowances. In FBiH, the following were not included: general water contribution (0.5% of net salary), disaster insurance contribution (0.5% of net salary), contribution for persons with disabilities (0.5% of gross salary), since these are not work-based contributions. Including these contributions would increase the tax wedge by 0.6 percentage points, for both calculations with and without meal and transport allowances, meaning that their inclusion would have a minimal effect on the level of the tax wedge.

Graph 4.5. Tax wedge (BiH²³⁵ and European OECD countries), individual with average salary, 2014



Sources: OECD Data²³⁶ and our own calculations

²³⁵ The presented tax wedge rate for BiH is the non-weighted average of entity tax wedge rates.

²³⁶ OECD Data, "Tax wedge," <https://stats.oecd.org/Index.aspx?DataSetCode=AWCOMP> (accessed on 25 October, 2015).

As opposed to the RS, where the tax wedge does not increase along with income, the tax wedge in FBiH is more progressive. This is attributed to non-taxable, fixed contributions such as the meal allowance, so the percentage of effectively non-taxable income decreases as income increases. Still, progressivity is not as significant for lower incomes.²³⁷ In other words, the tax burden for low-income workers is still very significant (40.15%), in contrast to the OECD countries where the average tax wedge is 32.2%.²³⁸

According to the World Bank, the key characteristic of tax structure in Bosnia and Herzegovina is reliance on labor taxation,²³⁹ which increases incentives for informality,²⁴⁰ i.e. unreported employment and thus leads to a large number of workers employed in the informal sector.²⁴¹ Other authors also note that the tax wedge probably has more influence on labor market performance, and on the informal economy in BiH, than minimum wages or employment protection legislation.²⁴²

In that respect, many current reform proposals pertain to reforming the tax structure and lessening the burden on employers by reducing the tax wedge. Reducing the labor burden is also announced in the Reform Agenda, primarily by reducing contributions for health insurance, while at the same time securing additional sources of funding to finance healthcare,²⁴³ reducing public spending, reforms of the healthcare sector, expansion of the tax base, etc.²⁴⁴ Similar measures have also been articulated in other recommendations and proposals.²⁴⁵

While reducing the tax wedge, especially lessening the burden on the lowest wages, is generally considered a good step towards improving the situation in the labor market,²⁴⁶ in this case it is not certain whether or not tax and contribution

²³⁷ See, for example: Arandarenko and Vukojević, *Labor Costs and Labor Taxes in the Western Balkans*; DG for Economic and Financial Affairs and Vienna Institute for International Economic Studies, *Adjustment capacity of labour markets of the Western Balkan countries*.

²³⁸ OECD Data, "Tax wedge."

²³⁹ The World Bank, *Bosna i Hercegovina: Izazovi i preporuke za reforme: pregled javnih rashoda i institucija* [Bosnia and Herzegovina: Challenges and Directions for Reform: A Public Expenditure and Institutional Review], Report No. 66253-BA (Washington: The World Bank, 2012), p. 31.

²⁴⁰ *Ibid.*, p. 32.

²⁴¹ *Ibid.*

²⁴² O'Higgins, "BiH: Wage trends and policies in response to the financial and economic crisis," pp. 69–70.

²⁴³ According to the Reform Agenda, "reduction of the burden on labour needs to be implemented by reducing contributions for health insurance, coupled at the same time with the need to ensure additional revenues for extra-budgetary funds to cover the losses generated as a result of the reduced contribution rate." "Reform Agenda for BiH," p. 2.

²⁴⁴ "Reform Agenda for BiH," p. 2.

²⁴⁵ See IMF, BiH: Letter of Intent, p. 7; EU Delegation to BiH, Compact for Growth and Jobs in BiH, pp. 5 and 11; Council of Ministers of BiH, National Economic Reform Programme for 2015, pp. 107 and 120.

²⁴⁶ Arandarenko and Vukojević, *Labor Costs and Labor Taxes in the Western Balkans*, pp. 58–59.

reforms will have a negative effect on workers' security (primarily unemployment benefits), as well as services such as health insurance. Also, although it is expected that the reduction in contributions could be compensated by expanding the tax base and through other sources of funding,²⁴⁷ Arandarenko and Vukojević point out that the financial implications of reducing contributions should be considered carefully. While expanding the tax base may be one way to compensate for losses in social funds, based on international experiences, one can expect that an increase in the number of insured persons paying contributions will not entirely compensate for the reduction in contributions per person.²⁴⁸

Also, as noted by Arandarenko and Vukojević, the overall effect of the tax wedge on employment cannot merely be equated to the effect of labor costs, given that it also depends on other factors, e.g. whether or not minimum wages are binding and on employers' and employees' relative bargaining power, as well as on the value that employees attribute to the benefits/services financed by social contributions or taxes.²⁴⁹ According to the study of the European Commission and the Vienna Institute for International Economic Studies, in terms of informal economy in relation to the tax wedge in BiH, the problem is not so much the cost of public services (or contributions paid for them), as is the actual supply of such services.²⁵⁰ In other words, motivation for employment in the formal sector also depends on the quality of public services in the realm of social security and healthcare.

Given the current uncertainty over whether work does (not) pay for low-wage earners, there is also the question of how low-paid workers could be stimulated to work in the formal sector, especially in view of the findings of some studies that the tax wedge itself is negatively correlated with the probability of informal sector employment, which indicates that it cannot sufficiently explain the lack of motivation for employment in the formal sector.²⁵¹ Usually, a few important measures are identified in this domain: reducing taxes for low-wage earners through policies such as wage subsidies, credits for covering social security contributions, in-work benefits or benefits conditional on employment (e.g. benefits in the form of cash transfers or formal employment-conditional, refundable income tax credits). On the other hand, it is important to take into account not just the marginal effective tax rate for individuals, but also the so-called formalization tax rate, which pertains not only to the disincentives for

²⁴⁷ World Bank, BiH: Challenges and Directions for Reform, p. 37.

²⁴⁸ Arandarenko and Vukojević, *Labor Costs and Labor Taxes in the Western Balkans*, p. 60.

²⁴⁹ *Ibid.*, p. 57.

²⁵⁰ DG for Economic and Financial Affairs and Vienna Institute for International Economic Studies, *Adjustment capacity of labour markets of the Western Balkan countries*, p. 90.

²⁵¹ Johannes Koettl and Michael Weber, "Does Formal Work Pay? The Role of Labor Taxation and Social Benefit Design in the New EU Member States," Discussion Paper No. 6313 (Bonn: IZA, 2012), p. 29; 5.

formal employment due to high taxes, but also to the loss of income-tested social benefits, including social assistance, family and housing benefits, etc.²⁵²

Current reform proposals in BiH generally do not reference other, similar reforms, such as effective coordination of labor taxation reforms with any increase in minimum wages, introducing in-work benefits as a measure to make work pay, or combinations with various types of tax deductions or credits. Although some reform proposals mention the possibility of introducing direct progressive income taxation, which could reduce the burden on the lowest wages, it is not clear what kind of solutions they offer.²⁵³ Also, given that in the context of reforming the tax wedge in FBiH, there is often mention of the possibility of taxing meal and other allowances, which currently in FBiH *de facto* reduce the tax wedge, this begs the question of whether such reforms would be combined with more comprehensive reforms of the tax system (e.g. with the introduction of progressive tax rates, a zero income tax rate for minimum wages) in order to help maintain a level of progressivity.²⁵⁴

4.3. Collective Bargaining Mechanisms and Social Dialogue

4.3.1. Key Discussions, Trends and Practices

The relationship between unions, employers, or social partners, and the state, go a long way in determining developments in the labor market. The nature of mechanisms for collective bargaining on working conditions, i.e. their structure and type of coordination are particularly important features of the labor market's institutional environment. Many countries, including BiH, have signed and ratified

²⁵² Koettl and Weber have shown that the higher the marginal effective tax rate, on the one hand, and the formalization tax rate, on the other, the greater the probability of informal employment. *Ibid.*, p. 29.

²⁵³ See, for example: Government of FBiH, *Ažurirani akcioni plan za realizaciju Reformske agende Federacije BiH* [Updated Action Plan for the Implementation of the Reform Agenda of the Federation of BiH], Sarajevo, December 2015, p. 2. For an overview of the debate for and against introducing progressive tax rates in BiH, see: Federal Institute for Development Programming (FIDP), *Analiza uvođenja diferenciranih stopa poreza na dohodak u FBiH* [Analysis of Introducing Differentiated Income Tax Rates in FBiH] (Sarajevo: FIDP, 2015). For more on the international debate on taxation systems in the context of financing the welfare state, see: Nathalie Morel and Joakim Palme, "Financing the Welfare State and the Politics of Taxation," *The Routledge Handbook of the Welfare State*, ed. Bent Greve (New York: Routledge, 2013), pp. 400–409.

²⁵⁴ See, for example, Arandarenko and Vukojević, *Labor Costs and Labor Taxes in the Western Balkans*, p. 61.

conventions of the International Labor Organization that define standards in freedom of association, tripartite consultations and collective bargaining.²⁵⁵

Collective bargaining mechanisms are a potentially powerful tool of public policy coordination within the economy.²⁵⁶ According to Cazes et al, collective bargaining is a process that determines the “employment relationship, in particular, wages, working time and working standards.”²⁵⁷ The process of collective bargaining can take place at the national (inter-sectoral) level, at sectoral or at company level. Although there are differences between countries, the most widespread is multi-level bargaining.²⁵⁸ Governments usually define the rules for collective bargaining, but social partners are also allowed a certain degree of self-regulation.

Given that working conditions are an important component of economic production, collective bargaining can have a direct impact on labor market and macroeconomic performance.²⁵⁹ However, just as with other labor market institutes, there are diverse understandings of its importance and potential impact on labor market performance.

In economic theory, it is usually thought that the unions themselves, by monopolizing labor supply, have a tendency towards increasing wages, and that consequently a high share of workers who are union members is expected to lead to increased unemployment,²⁶⁰ especially in the case of very elastic labor force supply. Strong unions are also linked to compressed wage structures,²⁶¹ which can reduce the chances of employment for low-skilled workers.²⁶²

Nevertheless, the positive effects of union organization on wage levels, working conditions and increased productivity have also been recognized. According to a World Bank report from 2003:

“Workers who belong to trade unions earn higher wages, work fewer hours, receive more training, and have longer job tenure on average, than their non-unionized counterparts [...] On the other hand, temporary layoffs can be more frequent in unionized firms. At the macroeconomic level, high unionization rates lead to lower inequality of earnings and

²⁵⁵ E.g. ILO Convention No. 144 on Tripartite Consultations, Convention No. 87 on Freedom of Association, Convention No. 98 on the Right to Organize and Collective Bargaining, and Convention No. 154 on Collective Bargaining. For full texts of the conventions, see the International Labor Organisation website: <http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12000:0::NO> (accessed on 17 December 2015).

²⁵⁶ Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, p. 25

²⁵⁷ *Ibid*, p. 5–6.

²⁵⁸ *Ibid*, pp. 5–6.

²⁵⁹ *Ibid*, p. 6.

²⁶⁰ Avdagic and Salardi, “Tenuous link,” p. 746. For example, according to the statistical analysis by Avdagic and Salardi (2013), union density is associated with unemployment, but the magnitude of the effect is shown to be relatively small. *Ibid*, pp. 753–754.

²⁶¹ Low-skilled and high-skilled workers are paid similar salaries.

²⁶² Rueda and Pontusson (2000) in: Avdagic and Salardi, “Tenuous link,” p. 746.

can improve economic performance (in the form of lower unemployment and inflation, higher productivity and speedier adjustment to shocks).”²⁶³

Also, unions and workers’ councils may create competitive advantage, e.g. by encouraging workers to accept organizational and technological changes.²⁶⁴

It is assumed that wage coordination mechanisms contribute to decreasing unemployment.²⁶⁵ In coordinated systems, where unions ought to internalize the externalities of wage policies, the expectation is that - in comparison to systems that have uncoordinated bargaining - real wages, and consequently unemployment, will be lower.²⁶⁶ Collective bargaining should help in adjusting the level of employment protection to economic restrictions in cases of macroeconomic shocks, while guaranteeing basic rights and working conditions.²⁶⁷ Still, the assumption is that collective agreements with longer duration increase nominal wage rigidity.²⁶⁸

Collective bargaining can also have significant redistributive effects. Studies have shown that, in advanced economies, coverage by collective agreements and centralization of bargaining reduces wage inequalities,²⁶⁹ but there are discussions on the dimensions of such effects. Empirical research has also shown that unions decrease the overall dispersion of wages in the labor market.²⁷⁰

In any case, notwithstanding the potential negative implications, the positive effects of collective bargaining mechanisms can be manifold. According to the ILO, economic systems that have social dialogue structures and processes bear the potential for resolving important economic and social matters, fostering good governance and advancing economic stability and progress.²⁷¹

Countries vary greatly in terms of unionization and collective bargaining: in the US, the UK, New Zealand and Japan, the rate of coverage by collective agreements corresponds to the unionization rate, so that a drop in union density results in a proportional decrease in coverage by collective agreements.²⁷² On the other hand, in many EU countries, collective agreements pertain to all workers and

²⁶³ World Bank (2003), in: Freeman, “Labor market institutions without blinders,” p. 134.

²⁶⁴ Regini, “The Dilemmas of Labor Market Regulation,” p. 26.

²⁶⁵ Avdagic and Salardi, “Tenuous link,” pp. 753–754.

²⁶⁶ Hall and Franzese (1998), in: Avdagic and Salardi, “Tenuous link,” p. 746.

²⁶⁷ Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, p. 25.

²⁶⁸ *Ibid.*, pp. 8–9.

²⁶⁹ Kahn (1998), in: Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, pp. 7–8.

²⁷⁰ Hayter and Weinberg (2011), in: Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, pp. 7–8.

²⁷¹ Freeman, “Labor market institutions without blinders,” p. 133.

²⁷² Union (membership) density or rate of unionization indicates the power of bargaining held by unions, while collective bargaining coverage relates to the breadth of application of collective agreements.

companies in a given sector, irrespective of the power of the unions. This pattern is most evident in France, where coverage by collective bargaining is among the world's highest, while the rate of unionization is very low.²⁷³

Since the 1990s, Western economies have seen a trend towards deregulation and decentralization despite the positive role of collective bargaining in facilitating the adjustment of enterprises to macroeconomic shocks and retaining jobs (e.g. through internal flexibilization).²⁷⁴ It, therefore, does not come as a surprise that this period of decentralization and deregulation is linked to a general increase in the inequality of wages.²⁷⁵ There is also a marked trend of significant decrease in union membership (see Table 4.3). Such trends are particularly evident in countries of Central and Eastern Europe, where union membership stopped being mandatory following the collapse of communism.²⁷⁶ While in the 1990s, there was still a high rate of unionization, and coverage by collective agreements and coordination were close to the OECD average,²⁷⁷ the early 2000s saw a significant weakening of collective bargaining and a drastic drop in union membership.²⁷⁸

²⁷³ Freeman, "Labor market institutions around the world," p. 6.

²⁷⁴ Hayter (2012) in: Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, p. 8.

²⁷⁵ Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, p. 8.

²⁷⁶ Avdagic and Salardi, "Tenuous link," p. 742.

²⁷⁷ Cazes and Nesporova, "Introduction," p. 42.

²⁷⁸ For example, while in the mid-1990s, the rate of unionization was above 50% in Bulgaria, Hungary, Slovakia and Slovenia, and close to 50% in the Czech Republic, in 2003, only Croatia and Slovenia reported a rate of unionization above 40%, while in all the other countries it had fallen to 20–35%. Coverage by collective agreements is generally higher than the rate of unionization, but in most countries it is below 50%. Only Slovenia has a high rate of coverage by collective agreements of 98%. For more, see Cazes and Nesporova, "Introduction," p. 43. Data from later years shows that both the rate of unionisation and coverage by collective agreements have continued to decline.

Table 4.3. Unionization and collective bargaining trends in Europe

	Union density (0–100)			Centralization of bargaining (1–5)			Bargaining coverage (0–100)		
	1990–1994	2004–2008	Change	1990–1994	2004–2008	Change	1990–1994	2004–2008	Change
Austria	44,26	31,48	-28,87%	3,00	2,40	-20,00%	98,00	99,00	1,02%
Belgium	54,44	52,98	-2,68%	3,60	3,40	-5,56%	96,00	96,00	0,00%
Czech Republic	57,95	18,94	-67,32%	2,80	2,00	-28,57%	63,30	44,18	-30,21%
Denmark	76,34	69,90	-8,44%	3,00	2,60	-13,33%	84,00	80,90	-3,69%
Finland	77,46	71,04	-8,29%	4,20	3,80	-9,52%	81,60	90,00	10,29%
France	9,54	7,68	-19,50%	2,00	2,00	0,00%	91,60	90,00	-1,75%
Germany	32,66	20,72	-36,56%	3,00	2,40	-20,00%	71,20	63,28	-11,12%
Greece	35,30	24,46	-30,71%	3,60	3,60	0,00%	68,00	65,00	-4,41%
Hungary	83,10	17,02	-79,52%	2,00	2,00	0,00%	-	35,64	-
Iceland	86,95	79,40	-8,68%	-	-	-	60,00	46,54	-22,43%
Ireland	56,04	36,02	-35,72%	4,80	4,00	-16,67%	92,85	88,23	-4,97%
Italy	38,86	33,56	-13,64%	3,00	3,00	0,00%	82,40	80,00	-2,91%
The Netherlands	24,82	20,46	-17,57%	3,40	3,20	-5,88%	83,67	83,96	0,35%
Norway	58,10	54,36	-6,44%	4,20	3,60	-14,29%	71,00	73,37	3,33%
Poland	31,62	17,26	-45,41%	1,00	1,00	0,00%	-	38,13	-
Portugal	26,86	20,94	-22,04%	2,80	2,80	0,00%	75,00	59,08	-21,23%
Slovakia	67,30	20,60	-69,39%	2,20	1,60	-27,27%	-	43,00	-
Slovenia	61,10	29,70	-51,39%	2,40	4,00	66,67%	100,0	96,40	-3,60%
Spain	15,86	15,12	-4,67%	3	3	0,00%	84,38	86,25	2,22%
Sweden	84,76	73,54	-13,24%	3,60	2,40	-33,33%	89,00	92,50	3,93%
Switzerland	22,82	18,90	-17,18%	2	2	0,00%	48,00	48,00	0,00%
United Kingdom	37,62	28,48	-24,30%	1,00	1,00	0,00%	17,90	13,52	-24,47%

Source: Adapted from Visser (2011), presented in Avdagic and Baccaro, 2015²⁷⁹

According to Cazes et al, collective bargaining has been the casualty of the economic crisis, and in many European countries, the trend towards decentralization and fragmentation of relations between unions and employers

²⁷⁹ The rate of unionization or union density rate represents net union membership as a proportion of employed wage and salary earners. The index of bargaining centralization relates to the main level at which bargaining occurs. Moreover, bargaining coverage relates to employees who are covered by bargaining agreements as a proportion of all employed wage and salary earners who have the right to bargaining. Sabina Avdagic and Lucio Baccaro, "The Future of Employment Relations in Advanced Capitalism: Inexorable Decline?" In *The Oxford Handbook of Employment Relations: Comparative Employment Systems*, eds. Adrian Wilkinson, Geoffrey Wood and Richard Deeg (Oxford: Oxford University Press, 2015), p. 705.

has been accelerated.²⁸⁰ The primary rationale for this trend has been the assumption that greater coverage by collective agreements and more centralized bargaining have a negative effect on aggregate employment, and that social dialogue may stand in the way of austerity measures to combat the crisis,²⁸¹ but this mostly runs against the findings of previously cited studies in this domain. The implemented reforms have promoted decentralization and/or deregulation of collective bargaining, by introducing, for example, opt-out clauses in sectoral agreements that allow for an easier exit from such arrangements, or by giving legal validity to bargaining at the company level. In many cases, workers' rights to representation have been reduced by reforms through stricter conditions for establishing a trade union or by restricting the ability to call a strike. Given the empirical evidence of the harmfulness of fragmentation of collective bargaining, some authors believe that a continued trend in this direction is not likely to lead to an increase in employment.²⁸²

4.3.2. Social Dialogue and Collective Bargaining in Bosnia and Herzegovina

The institutional framework for tripartite social dialogue in BiH is made up of economic-social councils at the level of FBiH²⁸³ and RS,²⁸⁴ the Brčko District²⁸⁵ and the FBiH cantons. The economic-social councils were founded on the basis of valid labor legislation, while the collective bargaining system for which they are authorized is guaranteed under the Constitution of BiH, the European Social

²⁸⁰ This trend of reduction has been noted in Ireland, Cyprus, Slovakia, Bulgaria, Estonia, Slovenia, Hungary, Spain, Malta, the Czech Republic, Poland, Germany, The Netherlands, Denmark, Sweden, the United Kingdom, Luxembourg, and Belgium. It has remained the same in Greece, Finland, France, Italy, and Switzerland. An increase has been noted in Austria, Iceland, Lithuania, Portugal, and Latvia. For more, see: Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, pp. 12–13 and 25.

²⁸¹ Cazes, Khatiwada and Malo, *Employment Protection and Collective Bargaining*, pp. 12, 20, 22–23.

²⁸² *Ibid.*, pp. 12, 22–23.

²⁸³ The FBiH Economic-Social Council (BCS: Ekonomsko-socijalno vijeće, ESV FBiH) was founded in 2002 by the Agreement on the the Economic-Social Council for the territory of FBiH. According to this Agreement, ESV FBiH has 18 members, of which each social partner independently appoints 6 representatives and each representative has a deputy. ESVF BiH is obliged to hold regular sessions at least once every 90 days. "Sporazum o ekonomsko-socijalnom vijeću za teritoriju FBiH," *Official Gazette of the Federation of BiH* 47/02, 42/03, and 08/08, Articles 6 and 10. Apart from the council at the entity level, there are also economic-social councils in a number of cantons in FBiH.

²⁸⁴ The Economic-Social Council at the RS level (BCS: Ekonomsko-socijalni savjet, ESSRS) was founded by an Agreement in 1997, and in 2008, the Law on the Economic-Social Council was enacted. ESSRS comprises 9 members, with each social partner appointing three representatives and where each member has a deputy authorized to replace the member in the work of the Council with the same rights and obligations whenever the member is unable to attend the Council sessions. "Zakon o Ekonomsko-socijalnom savjetu," *Official Gazette of Republika Srpska* 110/08, Article 6.

²⁸⁵ The Economic-Social Council in the Brčko District was established in 2011 by virtue of the Agreement on the Establishment of the Economic-Social Council in the Brčko District of BiH.

Charter, conventions of the International Labor Organization (Conventions No. 87, 98, and 144), and entity labor laws.²⁸⁶ The economic-social councils in BiH are responsible for establishing and developing social dialogue of significance for the socio-economic position of social partners, monitoring and evaluation of social and economic trends and policies, proposing changes and/or adjustments of relevant policies and practices, considering and providing opinions on drafts of relevant regulations, encouraging amicable labor dispute settlements, etc. They are made up of representatives of unions, employers and governments at various levels.

Still, the system of collective bargaining in its current form in BiH is relatively new, given that in the former Yugoslavia, state authorities and unions determined the working conditions within a self-management system. Hence, the social dialogue institution in BiH does not have a developed tradition, level of efficiency or social significance as in some European countries. It is believed that unions do not have a firm autonomous position as social partners,²⁸⁷ and that despite a nominally high unionization rate in BiH (see Graph 4.6), they cannot mount the desperately needed counter-balance to interests of capital, which is the main precondition for genuine social dialogue. In addition, some of our semi-structured interview respondents pointed out that the backbone of social dialogue should be negotiations, consensus and coordination between employers and unions, with a less prominent role of the government, which is, in their opinion, currently too dominant. When it comes to the participation of employers in social dialogue, some of the interviewees were of the opinion that the representation of one portion of businesses, particularly those from the private sector, in economic-social councils is inadequate, and that social dialogue thus does not provide adequate representation for the interests of all businesses. The majority of interviewees agreed that it was necessary to further improve the activities and functions of economic-social councils by strengthening social dialogue in BiH.

According to Arandarenko and Vukojević, although it seems that the role of unions and collective bargaining mechanisms is generally limited and that it is further diminishing in Western Balkan countries, countries with general collective agreements, such as BiH, Montenegro and Macedonia, tend to have higher rates of unionization and greater union influence over processes of wage determination,

²⁸⁶ Goran Stanković, "Annual Review of Labour Relations and Social Dialogue in South East Europe: 2013: Bosnia and Herzegovina," *Labour Relations and Social Dialogue in South East Europe* (Belgrade: Friedrich Ebert Stiftung, 2014) and ILO, Decent Work Country Programme Document 2012–2015: Bosnia and Herzegovina, p. 6. According to the ILO report, BiH has not ratified Convention No. 154 on Collective Bargaining.

²⁸⁷ See Belma Buljubašić, "Iznevjerena tradicija: kratak osvrt na istorijski razvoj sindikalnih organizacija u BiH" [A Tradition Betrayed: A Brief Review of the History of Trade Unions in BiH], in *Lice i naličje socijalne pravde u Bosni i Hercegovini* [Two Faces of Social Justice in Bosnia and Herzegovina] (Sarajevo: Open Society Fund BiH, Peace Academy Foundation, 2014), as well as Hartmut Lehmann and Alexander Muravyev, *Labor Markets and Labor Market Institutions in Transition Economies* (Bonn: IZA, 2011), pp. 7–8.

than those with decentralized bargaining, such as Albania and Serbia. Still, as the authors point out, most countries exhibit a clear tendency towards duality of the formal labor market between a more regulated public and a less regulated private sector, irrespective of formal coverage by collective agreements,²⁸⁸ which is also often noted in the case of BiH.

Although there is no official data on the unionization rate in BiH, according to some unofficial estimates²⁸⁹ and our calculation, based on data on approximate membership in leading federations of unions,²⁹⁰ it can be assumed that the rate is somewhere between 50% and 60%. However, this estimate should be taken with reservation for a number of reasons. First of all, there is no official and regularly updated data on union membership in BiH.²⁹¹ In addition, the majority of union members are public sector employees, while the unionization of workers in the private sector is significantly lower, and there is, thus, a discrepancy in the unionization and representation of workers' interests between these two sectors.²⁹² Finally, registered unemployment data were used when calculating the unionization rate, while those employed in the informal labor market were not taken into account, even though it is assumed that the share of informal employment within total employment is significant.²⁹³ By this rough

²⁸⁸ Arandarenko and Vukojević, *Labor Costs and Labor Taxes in the Western Balkans*, p. 40.

²⁸⁹ Duljko Hasić, "Annual Review of Labour Relations and Social Dialogue in South East Europe 2014: Bosnia and Herzegovina," *Labour Relations and Social Dialogue in South East Europe* (Bratislava: Friedrich Ebert Stiftung, 2014), p. 12.

²⁹⁰ The three largest unions in BiH have a total combined membership of around 362,600. According to the data available on the official website of the Confederation of Independent Trade Unions of BiH, this Confederation brings together 24 branch unions with total combined membership of 230,000 [available at: Confederation of Independent Trade Unions, "O nama" [About us], http://www.sssbih.com.ba/index_files/page356.htm (accessed on 17 December, 2015)]. The Confederation of Trade Unions of Republika Srpska brings together 15 branch unions that, according to a statement released on 1 May, 2015, on its official website, had a total combined membership of 102,587 [available at: Confederation of Trade Unions of Republika Srpska, "Prvomajski proglašenje" [First of May Proclamation], <http://www.savezsindikatars.org/saopstenja.php> (accessed on 17 December 2015)]. In addition, there is a parallel Confederation of Unions in the RS with some 30,000 members [available at: Confederation of Unions of Republika Srpska, "Sindikatski savez" [Union], <http://www.ksrs.org/konfederacija-sindikata-republike-srpske/> (accessed on 17 December, 2015)]. Compared to the total number of employees in the territory of FBiH and RS – which according to the data of the Federal Institute for Statistics [<http://www.fzs.ba/> (accessed on 17 December, 2015)], was around 450,000 in 2014 and first half of 2015 (for complete and detailed monthly data on employment, see the official FZS website), and in the RS, according to the data of the RS Institute for Statistics [<http://www.rzs.rs.ba/> (accessed on 17 December, 2015)], it was around 240,000 (for complete and detailed monthly data on employment, see the official RZS website) – union members make up around 53% of the employed. However, given that there is no data on the number of members of the Union of the Brčko District of BiH, and that one can assume that unions that are not members of existing confederations are also active, the estimated rate of unionization may vary up to around 60%.

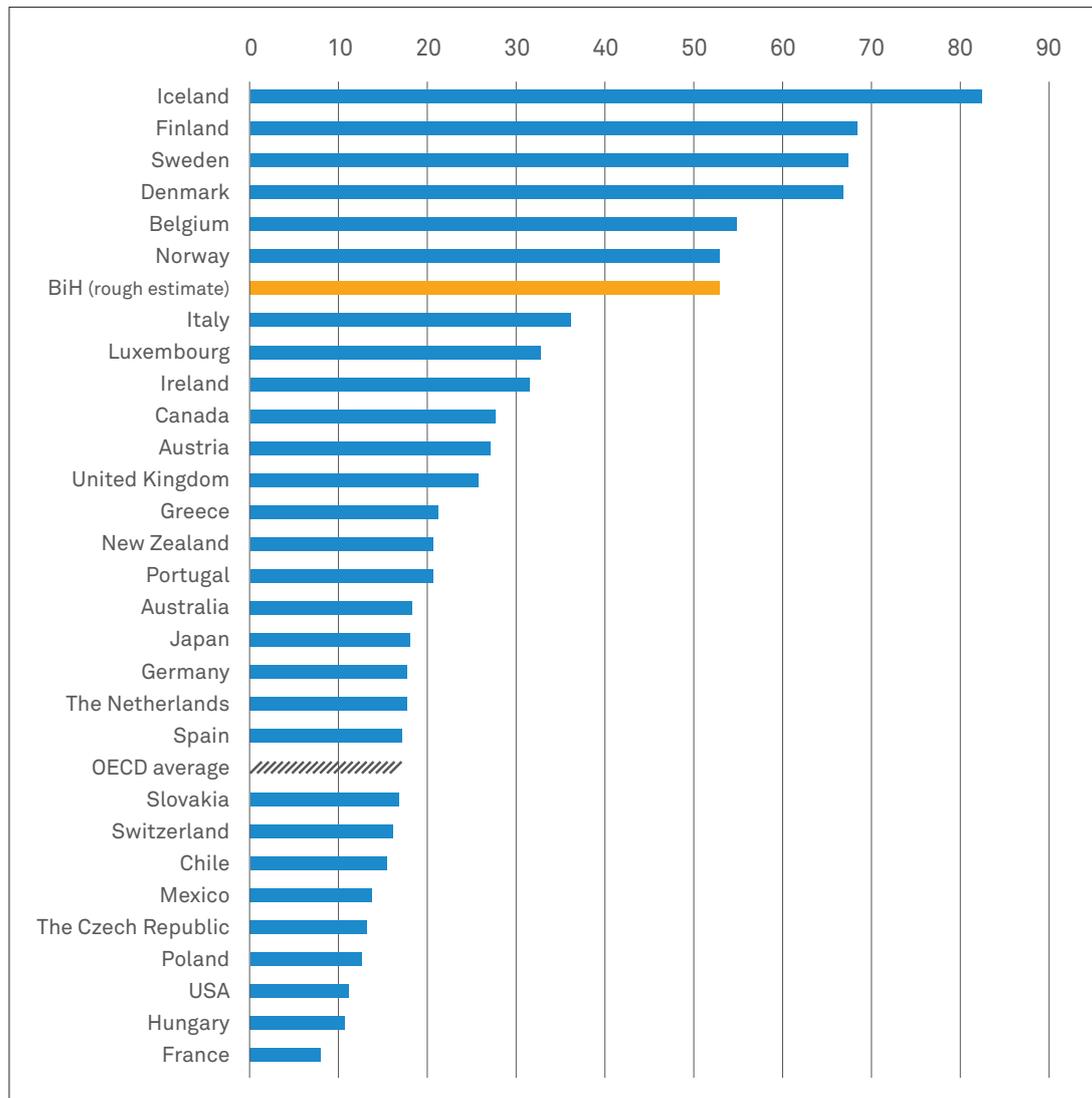
²⁹¹ See also Duljko Hasić, "Annual Review of Labour Relations and Social Dialogue in South East Europe 2014: BiH," p. 12.

²⁹² *Ibid.*

²⁹³ See: ILO, *Global Employment Trends 2013*, p. 60.

and conditional estimate, the unionization rate in BiH is much higher than the average in OECD countries, for instance. The average unionization rate in these countries in 2012 and 2013 was about 17%, while Norway, Belgium, Denmark, Sweden, Finland and Iceland had a unionization rate of 50% or more.

Graph 4.6. Rate of unionization in BiH and OECD countries in 2012



Sources: our calculations and OECD²⁹⁴

When it comes to collective agreements in BiH, according to the current labor laws,²⁹⁵ they can be signed in the form of a general collective agreement for the territory of an entity or the Brčko District, a branch collective agreement for the

²⁹⁴ OECD Stat, "Trade Union Density," https://stats.oecd.org/Index.aspx?DataSetCode=UN_DEN# (accessed on 17 December, 2015).

²⁹⁵ Labor Law of FBiH, Articles 137–149; Labor Law of Republika Srpska, Articles 158–169; Labor Law of BD, Articles 96–103.

territory of an entity or one or more cantons in FBiH, or as an individual collective agreement at the level of the company, or with an individual employer or a group of employers. The general collective agreement in FBiH is signed between the representative association of employers and the association of unions founded in the territory of this entity,²⁹⁶ while in the RS and BD, the government is also a party to the general collective agreement.²⁹⁷ The general collective agreement determines the basic working conditions, i.e. the labor rights and obligations of workers²⁹⁸ not defined in law, and they are applicable to all professions and economic sectors, so in the context of negotiating workers' rights, it may be considered the most important regulation next to the labor law.²⁹⁹ Branch collective agreements, which define working conditions specific to individual sectors of the economy, are signed in both entities by representative unions and employers' associations for one or more sectors or areas of business activity,³⁰⁰ while in the RS, the labor ministry may also be party to the agreement when social partners determine that such participation is necessary in order to achieve common aims in the realm of economic and social policy in the RS.³⁰¹ Finally, individual collective agreements are signed between one or more employers and a representative union, in order to determine the working conditions on the level of one or more business entities or a business unit.³⁰²

According to the current legislation in the entities,³⁰³ the working conditions determined by collective agreements in FBiH and RS are binding for the parties to the agreement at the time of the agreement and those that join it later, while the terms and applicability of collective agreements in BD are subject to the arrangements made by the parties entering such agreements. If there is interest

²⁹⁶ Labor Law of FBiH, Article 138, paragraph 1.

²⁹⁷ Labor Law of Republika Srpska, Article 161, paragraph 1; Labor Law of BDBiH, Article 96, paragraph 1.

²⁹⁸ E.g. minimal price of work, conditions related to the number and schedule of working hours, leave, terms of employment and termination of employment, etc.

²⁹⁹ See also Duljko Hasić, "Annual Review of Labour Relations and Social Dialogue in South East Europe 2014: BiH," p. 8.

³⁰⁰ Labor Law of FBiH, Article 138, paragraphs 2 and 3; Labor Law of Republika Srpska, Article 161.

³⁰¹ Labor Law of Republika Srpska, article 161, paragraph 3.

³⁰² Branch collective agreements may not determine less favorable working conditions, or a narrower scope of workers' rights compared to the general collective agreement, and individual collective agreements in turn may not determine less favorable working conditions than the relevant branch collective agreement.

³⁰³ Labor Law of FBiH, Article 142; Labor Law of Republika Srpska, Article 159, paragraph 1.

by entities, collective agreements may be expanded to include parties that were not included in the agreement at the time of its initial signing.³⁰⁴

With respect to the duration or applicability of collective agreements to their parties, the current legislation in the RS stipulates that the agreements may be concluded for a specified or unspecified duration.³⁰⁵ In FBiH, however, the latest changes to labor legislation preclude the possibility of concluding collective agreements of unspecified duration and limit their term to at most three years, with the possibility for extension of at most 90 days,³⁰⁶ i.e. for the duration of the bargaining period to conclude a new collective agreement. In the RS, each party may terminate the collective agreement with a termination notice of no less than 30 days (unless otherwise specified by the collective agreement),³⁰⁷ while in FBiH, the collective agreement may be terminated for the reasons, under the procedure and within the deadlines determined by the collective agreement.³⁰⁸

In BiH, collective bargaining is considered to be weak because of the lack of organized unions in the private sector (apart from those for formerly state-owned companies that have been privatized). Also, collective agreements do not apply to workers in the informal economy. In practice, coverage by collective agreements, particularly branch agreements, is limited in the private sector and applies mostly to the public sector, including public companies and privatized former public companies.³⁰⁹

According to a World Bank report for BiH, the current collective bargaining system in BiH is rigid and should be made more flexible, especially when determining labor prices in order to ensure easier procedures to change or temporarily suspend collective agreements so as to facilitate an adequate response to economic fluctuations and/or fiscal pressures when they arise.³¹⁰ In addition, the Letter

³⁰⁴ In FBiH, the federal minister for labor and social policy may, in consultation with the FBiH Economic-Social Council, “extend the application of the general and branch collective agreements to other employers who are not members of the association of employers - party to the collective agreement, for which it is determined to be in the interest of implementing economic and social policy in the Federation, with the aim of ensuring equal working conditions.” Labor Law of FBiH, Article 143. In the RS, the ministry responsible for labor may, in consultation with “the appropriate trade unions, employer or association of employers to whom the collective agreement is to be extended to,” “decide to extend the collective agreement, or particular provisions thereof, to legal persons that were not initially parties to the collective agreement and have not subsequently become parties to it,” provided that this is justified in the interest of achieving economic and social policy goals in the RS. In addition, the labor ministry in the RS may “at the initiative of parties to the collective agreement or whenever it finds it to be in the interests of RS, decide to exclude certain legal persons from the implementation of the collective agreement.” Labor Law of Republika Srpska, article 159.

³⁰⁵ Labor Law of Republika Srpska, Article 163.

³⁰⁶ Labor Law of FBiH, Article 140.

³⁰⁷ Labor Law of Republika Srpska, Article 163.

³⁰⁸ Labor Law of FBiH, Article 147.

³⁰⁹ O’Higgins, “BiH: Wage trends and policies in response to the financial and economic crisis,” pp. 66–67.

³¹⁰ See World Bank, *Bosnia and Herzegovina: Challenges and Directions for Reform*, p. 78.

of Intent to the IMF within the *stand-by* arrangement insists that the duration of collective agreements be limited, which has been done in FBiH through the adoption of the new Labor Law, and that sectoral collective agreements should apply only to those subjects that choose to join them,³¹¹ which would ultimately lead to relaxing collective agreements and greater liberalization of the labor market.

Still, there is currently no official data on the rate of coverage by collective agreements in BiH, and it is not clear to what extent they are actually applied in practice. Therefore, it is difficult to assess the level of rigidity of collective agreements in practice. Possible rigidities are usually associated with the application of collective agreements in the public sector: it is suggested that particularly during the economic crisis and the fiscal consolidation that followed, collective agreements made lay-offs and pay reductions more difficult in the public sector and public institutions had to bear high costs of legal disputes in this realm. For example, following the adoption of the *stand-by* arrangement with the IMF, in FBiH, added emphasis was placed on reducing public spending and limiting expenditure on wages. According to some authors, in practice, there has been reduction of non-taxable allowances, but average wages in the public sector were not significantly reduced.³¹² On the other hand, in the RS, the effects of the crisis were manifested more through lay-offs (usually as so-called “technological redundancies”) than through wage reductions, and through failures to pay social security contributions in some sectors.³¹³

Finally, it should be noted that current reform proposals do not express tendencies to improve the collective bargaining process, including improvements to the coordination between employers and unions at various levels and strengthening their role in developing important sectoral policies. This is a significant shortcoming if we take into account the potential positive effects of collective bargaining in the form of helping enterprises adjust to economic shocks, reducing pay inequality and unemployment.

4.4. Employment Policies

4.4.1. Passive Employment Measures

Unemployment benefits are one of the key elements to combat risk in the labor market. Two types of benefits can be distinguished. Unemployment insurance is paid to unemployed persons who had been employed in a given period for a certain minimum duration and had a certain minimum of paid contributions. On the other hand, unemployment assistance is a measure to prevent poverty in case

³¹¹ IMF, BiH: Letter of Intent, p. 10.

³¹² O’Higgins, “BiH: Wage trends and policies in response to the financial and economic crisis,” p. 77.

³¹³ Ibid, p. 78.

of unemployment and is conditioned on the income of the person, and is a part of the system of social protection. It is usually paid to the long-term unemployed with low income and who were not entitled to or are no longer entitled to unemployment insurance benefits. A minimum duration of employment or paid contributions is usually not a precondition or the required period of employment is shorter than for insurance benefits.³¹⁴ Both are considered types of passive employment measures, though in practice they are usually combined with efforts to activate the unemployed, by, for instance, being conditioned on job seeking or participation in employment programs.

From a macroeconomic perspective, passive employment policies act as automatic stabilizers and can thus “smooth out” aggregate economic shocks. If well designed, conditions of entitlement for benefits guarantee sufficiently wide coverage (i.e. share of the unemployed receiving benefits) to provide income security, and thus have a stabilizing role in the economy.³¹⁵

Still, it is believed that unemployment benefits can reduce motivation for work and job seeking, i.e. have disincentive effects, create “unemployment traps” and “inactivity traps,” as well as benefit dependence associated with long-term unemployment and reduced employability. In the case of “unemployment traps,” the unemployed are not prepared to accept employment if they are to earn a low net income gain compared to what they receive in benefits. Low-wage workers are particularly susceptible to this problem and usually make up the larger share of the unemployed. Similarly, in the case of “inactivity traps,” persons receiving means-tested social assistance as income replacement (typically the unemployed with an insufficient job tenure or contributions period, the long-term unemployed and those who are difficult to employ) are not prepared to take employment if they are to earn a low net income gain compared to the amount of assistance they receive. Inactivity traps raise the risk that persons will not return to the labor market and contribute to structural unemployment.³¹⁶ The risk of dependence on benefits increases with their duration and is greater if replacement rates³¹⁷ do not decrease during the unemployment period, and when job seeking conditions and availability for participation in various employment programs are insufficient or do not exist.³¹⁸

In other words, the way in which benefits are designed may increase or decrease the risk of low motivation to accept employment, as well as benefit dependence. Theoretical models in this domain predict that more generous benefits reduce the probability that beneficiaries will find a job and extend

³¹⁴ Klara Stovicek and Alessandro Turrini, “Benchmarking Unemployment Benefits in the EU,” Policy paper No. 43 (IZA, 2012), p. 5.

³¹⁵ Ibid pp. 4 and 6.

³¹⁶ Ibid, pp. 4, 6–7.

³¹⁷ Ratio of income from unemployment benefits and income received while employed.

³¹⁸ E.g. availability for participation in active employment measures, availability for occupational and geographic mobility, etc. Stovicek and Turrini, “Benchmarking Unemployment Benefits in the EU,” p. 7.

the period of unemployment. When replacement rates are high, the cost of unemployment is lower.³¹⁹ Also, given the potentially higher reservation wage,³²⁰ the unemployed may be less prepared to actively seek employment and accept jobs that are available.³²¹ The assumption that generous benefits contribute to unemployment because they negatively affect the motivation of the unemployed has been confirmed by many research studies, but mainly in terms of the duration of the period of receiving unemployment benefits. In other words, unemployed persons will be less motivated to return to the labor market if they receive unemployment benefits for a longer period of time.³²² On the other hand, some studies have found that the duration of unemployment benefits has a negative effect on all labor market indicators apart from aggregate unemployment, and this is mostly the case in OECD countries where benefits systems are more generous.³²³ Such findings potentially suggest that in the context of generally low demand for labor, less competitive individuals are compelled to receive benefits as long as possible (and/or engage in unreported employment). It is believed that long-term dependence on the benefits system contributes to lower participation in the labor market, and that it also leads to higher youth unemployment, long-term unemployment, and decreased employment.³²⁴

Still, given that reliable comparative quantitative data on the criteria for access to benefits are generally unavailable,³²⁵ research findings should be taken with reservation. For example, it is typically assumed that all unemployed persons have access to a certain level and duration of benefits, but in reality, access is commonly denied to those who have not paid a minimum of contributions towards insurance, or lack the required prior job record. Benefits may also be postponed or completely withheld if the person quit or was laid off for certain reasons. Also, access to benefits may depend on conditions such as active job seeking and accepting appropriate job offers. The obligation to search for a job

³¹⁹ The difference between the wage and the unemployment benefit.

³²⁰ The wage at which an unemployed person would be prepared to accept a job offer.

³²¹ E.g., Nickell (1997), Holmlund (1998), in: Avdagic and Salardi, "Tenuous link," pp. 745–746.

³²² Stovicek and Turrini, "Benchmarking Unemployment Benefits in the EU," p. 4. According to analysis by Avdagic and Salardi, their finding that generous benefits may play a role in unemployment is less stable and depends on specifications, and the magnitude of such effect is found to be relatively small. *Ibid.*, pp. 753–754.

³²³ Cazes and Nesporova, "Introduction," p. 54.

³²⁴ *Ibid.*

³²⁵ As noted by Venn (2009), numerous studies in this domain still focus on replacement rates, adjusted for maximum benefit duration, as an indicator of benefit generosity, and on expenditure on ALMPs or the rate of participation in ALMPs as an indicator for the strictness of active job-seeking requirements. Such indicators usually have a negative correlation with the strictness of entitlement conditions for access to unemployment benefits and fail to provide a complete picture of benefit generosity and activation policies in each country. Danielle Venn, "Eligibility Criteria for Unemployment Benefits: Quantitative Indicators for OECD and EU Countries," Working Paper No. 131 (Paris: OECD, 2012), p. 9, 25.

and other conditions are usually accompanied by sanctions, such as reducing or suspending benefits if the requirements are not met.³²⁶ As noted by Venn, numerous studies also indicate factors other than the replacement rates and the duration of benefits, as credible explanations for unemployment duration and/or benefit dependence.³²⁷ For example, job search conditions may affect the reservation wage and/or the intensity of job seeking among beneficiaries. Some studies have confirmed that specific conditions, such as regular reporting to the competent service on job-seeking efforts, lead to shorter unemployment, which is usually attributed to greater efforts in job seeking.³²⁸

Models of unemployment benefits differ in terms of the eligibility conditions for benefits, principles to determine their level and duration, as well as in terms of how they are financed and administrated.³²⁹ Esser et al. have identified the following models in European countries:³³⁰

- **Voluntary state-subsidized programs:** Also the earliest form of unemployment benefits, where insurance in the event of unemployment is administered by unions and mutual associations that offer benefits within funds financed from membership fees. The basic elements of such schemes may be found in the voluntary programs of Nordic countries, where the right to benefits depends on voluntary membership, and is usually supplemented with contributions to unemployment insurance funds. The state has the role of supervisor and regulator, but also usually contributes to financing benefits through subsidies, particularly in times of crisis.
- **Targeted programs:** Eligibility is based on assessment of need and benefits are disbursed at minimum levels, usually for longer periods. No EU country today relies solely on this model; instead, such programs are supplementary to regular insurance benefits and are paid to those who are no longer eligible or do not qualify for insurance benefits.
- **Mandatory unemployment insurance programs (comprehensive):** Entitlement to benefits is usually based on contributions. In the case of **comprehensive basic security**, benefits are flat-rate (e.g. Ireland, Malta, the United Kingdom) and such models typically have broad coverage because they include different profiles of workers, although entitlement depends on the amount of prior contributions and other criteria. In the case of **comprehensive income security** (e.g. Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Portugal, Romania, Slovakia, Slovenia³³¹),

³²⁶ Venn, "Eligibility Criteria for Unemployment Benefits," p. 7.

³²⁷ Ibid, p. 8.

³²⁸ Ibid, pp. 7-8.

³²⁹ Ingrid Esser et al, *Unemployment Benefits in EU Member States* (Brussels: European Union, 2013), pp. 4-5.

³³⁰ Ibid, pp. 5 and 7.

³³¹ Except that in Slovenia there are no ceilings on the amount of benefits.

benefits are adjusted to income levels, but there are maximum ceilings, sometimes to such an extent that they appear to be flat-rate in practice. Coverage should be similar to basic security programs, but the level of benefits should be higher on average, since they are predicated on income.

- **Mandatory unemployment insurance programs (corporatist):** In continental countries (e.g. Germany, Austria), state unemployment insurance programs are jointly administrated by representatives of employers and workers. Statutory income protection varies across occupations, but such differences have been reduced by harmonizing conditions for eligibility and benefit levels; in most countries, the rates of contribution are equal for all groups of workers. While categories of workers with weak labor market attachment were traditionally excluded, this has been changing over time. The benefit levels should be similar to those in comprehensive income security programs.³³²

Although these are complex programs,³³³ some authors have attempted to classify countries based on the type of benefit, relying on the Esping-Andersen typology (Table 4.4)³³⁴

³³² Esser et al, Unemployment Benefits in EU Member States, pp. 5 and 7.

³³³ Ibid, p. 7.

³³⁴ This taxonomy is proposed by the European Commission (2007), in: Stovicek and Turrini, "Benchmarking Unemployment Benefits in the EU," p. 9.

Table 4.4. Classification of states based on unemployment benefits systems

State model	Nordic	Continental	Anglo-Saxon	Southern	Central-Eastern
State	Denmark, Finland, the Netherlands, Sweden	Austria, Belgium, Germany, France, Luxembourg	Ireland, United Kingdom, Malta, Cyprus	Spain, Italy, Portugal	Greece, Bulgaria, Czech Republic, Estonia, Hungary, Lithuania, Poland, Slovakia, Slovenia, Romania, Latvia
Type of system	Insurance and unemployment assistance	Insurance and unemployment assistance	Assistance benefits more widespread than insurance benefits	Insurance benefits, unemployment assistance less common	Insurance benefits, assistance less common, significant support in the form of needs-based social and housing assistance
Conditions	Flexible	Strict	Census based	Strict	Strict
Generosity / Coverage	Generous and very redistributive; broad coverage	Generous, shorter duration / lower replacement rates than the Nordic model; broad coverage	Flat-rate usually lower than with insurance, long-term payment; broad coverage	Depends on prior job record and contributions paid; poor coverage	Scarce, replacement rates may be high, but usually diminish after the first year of unemployment; poor coverage
Role of job-seeking and ALMPs	Significant, with strict job-seeking and availability requirements	Important	Strict job-seeking requirement, ALMPs less important	Minor job-seeking requirements, more pronounced condition of participation in ALMPs	Relatively strict requirements regarding job-seeking and active participation in ALMPs

Source: Stovicek and Turrini, 2012.³³⁵

States vary considerably when it comes to the specific design of criteria for access to benefits. According to Venn, entitlement conditions are the strictest in Italy and Portugal, where contribution and/or qualifying period requirements of two years or more coexist with sanctions for voluntary unemployment. In most EU states, the requirement is less than one year of employment and/or contribution (Bulgaria, Cyprus, Finland, France, Greece, Luxembourg, The Netherlands, Norway, Slovenia, the United Kingdom). In most other countries, the requirement is about 12 months, and in only a few it is over 12 months (Italy, Portugal, Slovakia, Belgium, Ireland).³³⁶ As noted by Esser et al, around half of EU countries

³³⁵ Stovicek and Turrini, "Benchmarking Unemployment Benefits in the EU," pp. 9–11.

³³⁶ Venn, "Eligibility Criteria for Unemployment Benefits," p. 15.

have qualification periods of 50–52 weeks.³³⁷ Voluntarily unemployed persons are not eligible for unemployment benefits in some countries (e.g. Estonia, Greece, Italy, Luxembourg, Denmark, The Netherlands, Portugal, Romania and Spain), in some they are subject to sanctions (Slovakia and Lithuania) or their benefits are reduced (Bulgaria and the Czech Republic), while in others benefits are postponed or suspended (e.g. Denmark, Malta, Poland).

Benefits systems are combined with job-seeking requirements and active labor market programs (ALMPs) in various ways. In most European countries, valid reasons for refusing job offers are limited (e.g. caring for a family, health reasons, low wage compared to benefits, average wage or previously earned wage), especially in cases of long-term unemployment. In some states, participants in ALMPs must be available for work and actively seek jobs, while in others they must only be available but not seek jobs, or are not required to be available. Professional and geographic mobility, with prescribed exceptions,³³⁸ is also a condition in many countries. In most countries, those receiving unemployment benefits are subject to sanctions if they reject suitable job offers or participation in ALMPs without valid reasons, and benefits are suspended in countries with the strictest sanctions (e.g. Greece, Slovenia, Romania, Portugal, Slovakia). Also, there are models of increasing sanctions if beneficiaries reject suitable job offers or ALMP participation multiple times.³³⁹ Many countries impose a requirement to report to employment services on job seeking efforts and some have introduced individual counselling and job-search planning programs that are periodically evaluated (e.g. The Netherlands and Slovenia).³⁴⁰

European states have adopted different modalities for financing benefits. Generally speaking, in only a few countries are contributions paid solely by workers, while most foresee a combination of contributions from the insured worker and the employer. The state can have different roles: covering the deficit (e.g. Austria, Slovakia, Belgium), or subsidizing contributions (e.g. Germany, Greece, Slovenia, Spain, Denmark, Sweden), or partly or entirely covering flat-rate benefits (Luxembourg, Cyprus, Malta), or it may not contribute to financing at all (e.g. Estonia, France, The Netherlands, Bulgaria, Hungary).³⁴¹ The financing model in Austria is interesting: namely, contributions are paid to the worker's savings account, so that persons left without a job can access the contributions paid by employers as a percentage of salary. On the other hand, in Ireland, employers are compensated for 15% of the costs of severance pay through a special fund financed from social security contributions paid by employers and employees.

³³⁷ Esser et al, *Unemployment Benefits in EU Member States*, pp. 14–15.

³³⁸ E.g. the number of hours per day when a person is obliged to travel; in some countries, persons over 50 are not required to accept job offers in other occupations.

³³⁹ Venn, "Eligibility Criteria for Unemployment Benefits," pp. 15–20.

³⁴⁰ For a detailed assessment of the strictness of criteria for access to benefits, job-seeking and participation in employment programs for each country, see: *Ibid.*

³⁴¹ Esser et al, *Unemployment Benefits in EU Member States*, pp. 17–18.

The advantage of such schemes is that they do not pose additional obstacles in the case of dismissal or voluntary resignation, and offer security to workers, which is why they are seen as best practices in this realm.³⁴²

Variations in the generosity of unemployment benefits among EU member states are currently on the rise as a result of the recession and fiscal consolidation measures, which means that their stabilizing roles also differ.³⁴³ Esser et al. indicate a variation in gross replacement rates³⁴⁴ in the EU27³⁴⁵ for the average wage and single person family that range from 80% (Luxembourg) to 13% (United Kingdom), but are on average around 50% within the Eurozone and slightly below 40% outside the Eurozone. The formulas determining benefits have remained relatively stable in the past few decades, while earnings ceilings substantially fall behind wage increases. For example, in Sweden, the formal replacement rate has remained 80% of wages for the first 200 days of unemployment, while effective replacement rates, given the earnings ceilings, have dropped 13 percentage points between 2005 and 2010 alone. On the other hand, the earnings ceiling in Belgium has been increased, which has led to an increase in the effective replacement rate of 10 percentage points between 2005 and 2010.³⁴⁶ Net replacement rates are usually higher than the gross replacement rate due to the progressive nature of income tax,³⁴⁷ particularly in countries where benefits are non-taxable or exempt from contributions. Due to differences in taxation, the rates range between 92% (Portugal) to 12% (United Kingdom), and are on average 60% within the Eurozone.³⁴⁸ The duration of insurance benefits in the EU27 ranges from 21 weeks in Lithuania to an unlimited period in Belgium;³⁴⁹ in Eurozone countries, it is longer than two years, and in non-Eurozone countries it lasts around 30 weeks. In almost all countries, the duration of benefits is at least

³⁴² OECD, *Employment Outlook 2013*, p. 79.

³⁴³ Esser et al, *Unemployment Benefits in EU Member States*, p. 4.

³⁴⁴ Include income tax. Useful for differentiating between flat-rate and income-based insurance benefits.

³⁴⁵ EU states, except for Croatia.

³⁴⁶ Esser et al, *Unemployment Benefits in EU Member States*, p. 9.

³⁴⁷ In almost half of the EU27 states, the difference between the gross and net replacement rate is more than ten percentage points.

³⁴⁸ Esser et al, *Unemployment Benefits in EU Member States*, p. 10.

³⁴⁹ In a number of countries, the duration may be extended depending on the age and prior job record of the insured person.

26 weeks.³⁵⁰ The coverage rate, that is, the percentage of the labor force covered by unemployment insurance, is on average around 73% in the EU27.³⁵¹

The organization of unemployment assistance programs not based on insurance differs in terms of transition between types of program and the treatment of such assistance: 15 EU countries provide specific support for unemployment which is means-tested, or is paid as flat-rate assistance. The remaining states do not differentiate between social assistance and unemployment assistance. Net replacement rates in most states are generally lower than insurance benefits and range from 60% (Portugal) to 7% (Slovakia). In many countries of Central and Eastern Europe, duration of such assistance is below one year (e.g. Estonia, Hungary, Slovenia), and replacement rates in these countries are lower than in the rest of the EU.³⁵²

Given that the economic crisis has led to increased unemployment in most European countries, and that states have at the same time introduced fiscal caps, the question arises of how to strike a balance between income security and motivating the unemployed to seek jobs. Esser et al. (2013) point out that reform paths in this domain are necessarily different given that passive employment measures operate in heterogeneous labor market institutional contexts.³⁵³ Other authors in this realm indicate the importance of designing significant elements of unemployment benefits in combination with active employment measures,³⁵⁴ which are further discussed below.

4.4.2. Active Labor Market Programs

Active labor market programs (ALMPs) refer to support in job seeking, training, creating new jobs in the public sector, employment incentives in the private sector, and self-employment. ALMPs are an integral part of activation strategies that, according to the OECD, aim to include as many people as possible into the effective labor force, neutralize the potentially negative effects of unemployment benefits and other related benefits on motivation for employment by making them contingent on active job seeking and participation in measures that aim to improve employability and manage employment services and other measures of the labor market, so as to effectively promote and support return to work.³⁵⁵

³⁵⁰ Esser et al, *Unemployment Benefits in EU Member States*, pp. 11–12.

³⁵¹ In five countries, coverage is above 95% (Finland, Ireland, Greece, Luxembourg and Sweden). Apart from basic benefits, Finland and Sweden also offer voluntary unemployment benefits subsidized by the state, which increases the rate of coverage. On the other hand, coverage in Romania is below 50%, and it is also relatively low in Italy, Slovakia, Spain and Portugal. Esser et al, *Unemployment Benefits in EU Member States*, pp. 15–16.

³⁵² Ibid, pp. 12–14.

³⁵³ Ibid, p. 4.

³⁵⁴ Stovicek and Turrini, “Benchmarking Unemployment Benefits in the EU,” p. 4.

³⁵⁵ Martin, “Activation and Active Labour Market Policies in OECD Countries,” p. 3.

For a long time, the concept of activation pertained solely to public spending on ALMPs with a view to reducing structural unemployment. Still, experiences of OECD countries from the 1970s and 1980s have shown that some states with modest spending on ALMPs had low unemployment rates, while others with much higher spending had high structural unemployment. It was recognized that ALMPs must be viewed in combination with unemployment benefits and conditioning benefits on job-seeking and participation in ALMPs; thus, the concept of activation was expanded to take into account these diverse institutes and their interactions.³⁵⁶ Studies in this domain confirm the complementary relationship between unemployment benefits and ALMPs, which has influenced a change in the discourse on the need to “shift” from passive to active employment measures.³⁵⁷

To date, a host of studies has attempted to estimate the influence of ALMPs on labor market performance,³⁵⁸ with varying results. As summed up by Kluve et al. (2007), based on a meta-evaluation of studies in this domain, evaluations of traditional training programs have a moderate probability of reporting positive impacts on employment following completion of the program. Incentives paid to the private sector, the work of employment services, and sanctions for refusal to participate in ALMPs show a significantly better effect: when evaluating such programs, there is a 40–50% greater probability that studies will report a positive impact in relation to training programs. On the other hand, when evaluating public sector employment programs, there is a 30–40% lesser probability that studies will report a positive effect on employment following the completion of the program. The evaluation indicates the importance of training programs, private sector incentive schemes, as well as the important role of employment services and sanctions in terms of viable ALMPs. In other words, an adequate combination of support services for job seeking, counselling and monitoring, as well as appropriate sanctions for failing to meet requirements could significantly improve the effectiveness of job seeking. Effectiveness could further be improved through combination with other ALMPs such as trainings and incentives. On the other hand, the suggestion is to abandon public sector employment programs, which are rarely effective and do not improve the employment chances of the participants.³⁵⁹ The profile of the participants is also important: ALMPs specifically targeted at youth usually have significantly poorer results than those targeting adults, and 40–60% less likelihood of positive effects being reported.

³⁵⁶ Ibid, p. 3.

³⁵⁷ E.g. such discourse was promoted by the 1994 OECD Jobs Study. Ibid, p. 4.

³⁵⁸ Martin, “Activation and Active Labour Market Policies in OECD Countries,” p. 8.

³⁵⁹ According to Kluve et al. (2007), such programs are justified only in the context of equity. Some countries have already redefined the aims of such programs: they should “increase employability” and not employment, which is empirically difficult to assess. Jochen Kluve et al, *Active Labor Market Policies in Europe: Performance and Perspectives* (Berlin: Springer-Verlag, 2007), p. 6.

Such findings suggest that it is more difficult to assist youth through ALMPs, but it is unclear whether or not such programs should be abandoned or redesigned.³⁶⁰

Active labor market programs are an important element of the *European Employment Strategy*³⁶¹ and are the focus of labor market policies in most European countries, particularly in the aftermath of the economic crisis that has led to increased unemployment. The OECD and the European Commission particularly promote adopting ALMPs and expanding activation strategies to include various groups that are inactive on the labor market but receive different benefits, such as persons with disabilities and long-term illness, the early retired, single parents and social assistance beneficiaries.³⁶²

In 2011, OECD countries spent on average 0.6% of GDP on active employment measures; 4% of the labor force participated in active and 5.6% in passive employment measures.³⁶³ Paradoxically, the level of spending per unemployed person is still not what it was before the crisis, and in the period from 2007 to 2010, spending on active employment measures per unemployed person dropped by 20% on average in OECD countries.³⁶⁴ Reduced spending is particularly pronounced in some countries with a high increase in unemployment, such as Spain and Ireland, which indicates that the pressures of fiscal consolidation in numerous countries could further exacerbate the situation in the labor market.³⁶⁵ Countries of Central and Eastern Europe are particularly weak in implementing ALMPs, and many point out the problem of a large share of the inactive working age population receiving long-term benefits with little motivation to find employment, which, in turn, is associated with the problem of low productivity and high share of workers in the informal sector.³⁶⁶ Cazes and Nesporova believe that, generally speaking, increased labor market flexibility in these countries, following transition, was not sufficiently compensated with stronger employment security.³⁶⁷

Countries design and apply active employment measures in various ways. Some, for example, opt to integrate employment services with services that administer unemployment benefits (e.g. Ireland, Norway, United Kingdom). There is also a trend to hire private employment agencies on performance-based contracts (e.g. the “JobPath” program in Ireland or the “Work Programme” in the UK). For example, within the British program, private employment agencies were hired under five-year contracts to provide employment services to long-

³⁶⁰ Kluve et al, *Active Labor Market Policies in Europe*, pp. 6–7.

³⁶¹ Viebrock and Clasen, “Flexicurity and welfare reform,” p. 312.

³⁶² Ibid.

³⁶³ Martin, “Activation and Active Labour Market Policies in OECD Countries,” p. 7.

³⁶⁴ Ibid, p. 8.

³⁶⁵ Ibid, p. 8.

³⁶⁶ Viebrock and Clasen, “Flexicurity and welfare reform,” p. 311.

³⁶⁷ Cazes and Nesporova, “Introduction,” p. 46.

term unemployed, youth and beneficiaries of disability benefits, and were paid based on continuous performance and in larger amounts for riskier clients, while public services work with the short-term unemployed. Still, designing, applying and monitoring contracts with private service providers proved to be extremely demanding in terms of cost-effectiveness and adequate targeting and employment of hard-to-employ categories.³⁶⁸

Decentralized employment services have proven to be very effective in some countries, such as Finland and Switzerland. For example, once some of the responsibilities for disbursing benefits to long-term unemployed in Finland were transferred from the state to the municipalities, more attention started to be devoted to effective activation, which has led to increased employment. In other words, Finland is a good example of how increased local responsibility for financing benefits and for the design and implementation of employment services can increase the motivation of local stakeholders to make ALMPs as effective as possible.³⁶⁹ On the other hand, Switzerland has a long tradition of decentralized responsibility for employment policies, with a network of employment services spread across 26 cantons. The Swiss approach combines relatively generous benefits with strict application of job-seeking requirements, relatively high spending on ALMPs and making-work-pay policies. Activation is an important measure in the national system of performance rating, and the publication of performance ratings of each employment service has helped raise the average performance in this realm.³⁷⁰

One of the key policies in this domain pertains to activating persons who receive non-active benefits, including disability benefits and single parent benefits. For example, in Norway, employment services were integrated with agencies that disburse benefits and provide coordinated services to all clients of working-age who are receiving income support, including occupational rehabilitation for persons with health conditions.³⁷¹ In the UK, stricter criteria for access to disability benefits were introduced based on capacity for work, which led to a reduction in the number of beneficiaries. As of 2008, lone parent beneficiaries with their youngest child aged 12 (later reduced to 7) are subject to job-search requirements.³⁷² Generally, experiences have shown that activation strategies may function well for persons receiving insurance-based benefits, and for single parents, provided that adequate childcare support is secured. Activating disability beneficiaries who have some work capacity has proven to be more difficult. There is also the question of whether (and how) this population should be activated, which should certainly be subject to a wider social discussion. Various measures

³⁶⁸ Martin, "Activation and Active Labour Market Policies in OECD Countries," p. 14.

³⁶⁹ Ibid, pp. 16–17.

³⁷⁰ Ibid, pp. 19–20.

³⁷¹ Ibid, p. 23.

³⁷² Ibid, p. 25.

are available to improve professional opportunities (e.g. rehabilitation, in-work support, coordination between the healthcare sector, employment services and employers, etc.).³⁷³

The experiences of different countries in applying active employment policies also show that they cannot be viewed independently from the situation in the labor market, the needs of various profiles of the unemployed, as well as other labor market institutes, such as passive employment measures. According to some authors, unemployment benefits may be conditioned on active job-seeking and other requirements only when there is sufficient demand for labor. When demand is low, the emphasis on the conditionality of benefits may have to be lowered, and spending on training programs, particularly for the long-term unemployed, increased.³⁷⁴ The issue of professional orientation of activation strategies should also be taken into account: experiences to date show that due to benefits being conditioned, many beneficiaries are forced to accept low-paid jobs that do not provide them with adequate opportunities for professional development and that will not lift them out of poverty. In other words, activation strategies should take into account job quality, possibly by combining counselling and training measures.

4.4.3. The Institutional Framework for Employment in Bosnia and Herzegovina

Employment policies in BiH are often assessed as inefficient, inadequate and non-compliant with current international standards, while insufficient capacity and lack of coordination have been identified as the key problems of the existing structure and operation of institutions in this domain.³⁷⁵

Low staff capacities and organizational inefficiency of public employment institutes in BiH partly hinder the efficient implementation of their basic functions and goals defined by the ILO Employment Service Convention (No. 88). For the sake of illustration, according to data from 2012,³⁷⁶ one employee of the employment institute working directly with beneficiaries is responsible for

³⁷³ Ibid, pp. 27-28.

³⁷⁴ Ibid, p. 26. Martin highlights that empirical evidence on the effectiveness of “work-first” vs. “train-first” approaches to activation in periods of high unemployment does not bear clear results. For a discussion, see Ibid, pp. 26-27.

³⁷⁵ Centers for Civic Initiatives (CCI), *Analiza politika zapošljavanja u BiH – nacrt* [Analysis of Employment Policies in BiH - draft] (Sarajevo: CCI, 2013), p. 7.

³⁷⁶ This chapter mostly uses data from 2012 for two reasons: (a) this is the year of the most recent available data for BiH from primary and secondary sources that include most of the relevant indicators; (b) for the sake of international comparability, given that data from international institutions such as the OECD, ILO, EUROSTAT, etc. on relevant indicators are mostly complete up to 2012, while data for 2013 and 2014 are often unavailable or available only for certain indicators, incomplete, unstructured, etc.

approximately 1.363 unemployed persons in FBiH, 836 in the RS, and 830 in BD,³⁷⁷ while according to ILO recommendations this ratio should be 1:100.³⁷⁸ Given that there has been no significant decrease in employment in the meantime, it is safe to assume that these ratios are not considerably different today.

This situation is further complicated by the existing model of servicing health insurance for the unemployed through employment institutes, characteristic of some other Western Balkan countries as well,³⁷⁹ which diminishes the quality of service provision to job-seekers.³⁸⁰ Burdening employees at the institutes with administrative tasks related to managing health insurance records further diminishes the already scarce capacities of the institutes for active mediation between employers and the labor force.³⁸¹

That is why NERP foresees restructuring unemployment records, so that in FBiH “persons registered for the sake of exercising some other rights (e.g. right to health insurance) instead of active job search will not be registered in the unemployment records,”³⁸² while in the RS, the plan is to provide for “records of the unemployed persons, registered in the Employment Institute of Republika Srpska because of health insurance, to be kept in the Health Insurance Fund, since they do not make active supply of labor force.”³⁸³ Still, the question remains what will be offered as an alternative for persons without health insurance on any other grounds in FBiH and whether they will be left without health insurance altogether.

Apart from organizational inefficiency and insufficient staffing of public employment institutes, financial support for employment policies and programs in BiH is very low. During 2012, some 154,792,916 BAM³⁸⁴ were spent on the

³⁷⁷ Elmira Pašagić, Siniša Marčić, Adis Arapović, Efikasnost politika zapošljavanja u Bosni i Hercegovini: prepreke i šanse [Efficiency of Employment Policies in Bosnia and Herzegovina: Obstacles and Opportunities] (Sarajevo: Centers for Civic Initiatives, 2013), pp. 12, 32 and 47.

³⁷⁸ See: Employment and European Social Fund, Working papers on the contributions of Public Employment Services (PES) to combating long-term unemployment and local development (Brussels: European Commission, 2001), p. 28; as well as Diego F. Angel-Urdinola, Arvo Kuddo and Amina Semlali, *Public employment services in the Middle East and North Africa* (World Bank, 2012), p. 6.

³⁷⁹ See, for example: European Training Foundation (ETF), *Activating the Unemployed: Optimising Activation Policies in the Western Balkans and Turkey* (Turin: European Training Foundation, 2011), p. 23.

³⁸⁰ See *Ibid*, as well as the Council of Ministers of BiH, National Economic Reform Programme for 2015, p. 120.

³⁸¹ See Centers for Civic Initiatives, Analysis of Employment Policies in BiH; and Ranko Markuš and Bahrija Umihanić, “Public Employment Services Moving from Public Monopolies towards Quasi-Markets,” paper presented at the 7th *International Conference of the School of Economics and Business – Conference proceedings* (Sarajevo: School of Economics and Business, 2014), p. 313.

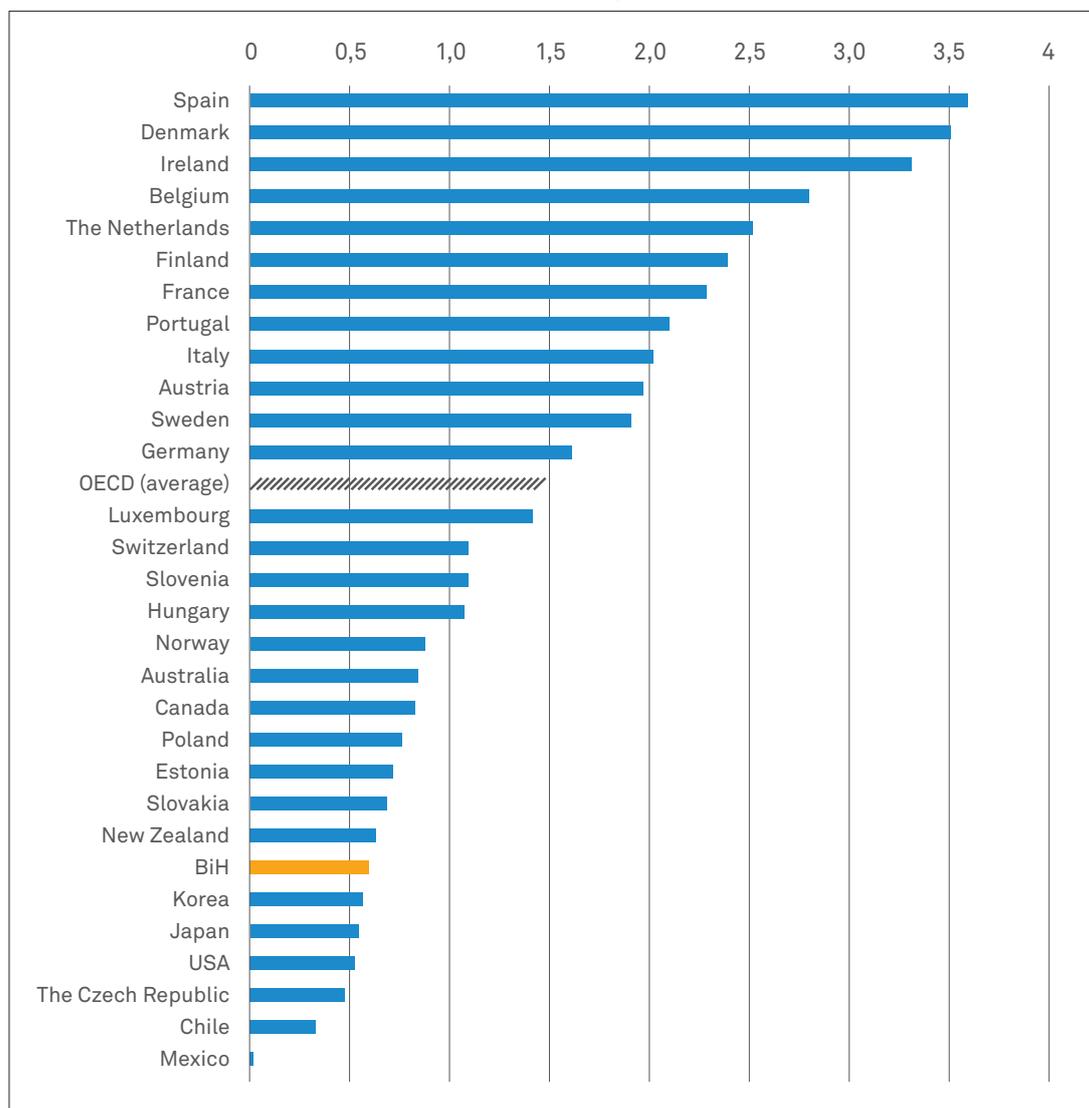
³⁸² Council of Ministers of BiH, National Economic Reform Programme for 2015, p. 120.

³⁸³ *Ibid*, p. 107.

³⁸⁴ Estimate based on data from Elmira Pašagić, Siniša Marčić and Adis Arapović, *Efficiency of Employment Policies in BiH*.

implementation of all the activities of the employment institutes, which is 0.59% of GDP.³⁸⁵ That same year, OECD countries on average spent 1.47% of GDP on employment, while this share is greatest in Spain, amounting to 3.6% of GDP.

Graph 4.7. Spending on employment measures in BiH and OECD countries in 2012 (% of GDP)



Source: OECD Data³⁸⁶

³⁸⁵ Nominal GDP in 2012 was 26,193,000,000 BAM. Source: Central Bank of BiH, "Glavni ekonomski indikatori" [Main Economic Indicators], http://statistics.cbbh.ba:4444/Panorama/novaview/SimpleLogin_bs.aspx (accessed on 17 December 2015).

³⁸⁶ OECD Data, "Social protection," <https://data.oecd.org/socialexp/public-spending-on-labour-markets.htm> (accessed on 17 December 2015).

Nevertheless, the most significant problem is the current prioritization and structure of spending for the implementation of employment policies. Employment institutes are primarily financed from unemployment insurance contributions.³⁸⁷ However, the allocation of funds for implementing active employment policy measures and mediation in employment in FBiH is carried out only if it is “determined that funds available to the employment service are sufficient to provide for the material and social security of unemployed persons and cover the administrative costs in the upcoming month,”³⁸⁸ where covering administrative costs of the service is of the highest priority.³⁸⁹ Pursuant to the Statute of the RS Employment Institute, regularly ensuring that unemployment beneficiaries have access to their rights (passive measures) takes priority in terms of allocation and use of funds available to the Institute, while any remaining funds are allocated to cover the costs of operation and administration of the Institute and implementing active employment policy programs and measures.³⁹⁰ No such prioritization has been prescribed in current legislation in the Brčko District.

When it comes to the structure of expenditures of employment institutes, out of the total of 157,792,916 BAM spent in 2012 in the entire territory of BiH, 20.5% was spent on administrative costs of the institutes, 58.4% on passive measures (monetary unemployment benefits, health insurance, bridging job tenure gaps, etc.), 20.1% on active measures and 1% on capital investments and other costs. An exception in the structure of expenditures in that year was the Brčko District, where more than 70% of total expenditure relates to active employment measures; still, in the period from 2008 to 2012, one can note that the share of costs on active measures out of total expenditure in the BD institute varies significantly.³⁹¹

³⁸⁷ To provide an example, about 90% of revenues of the public employment services in the period 2009–2013 in FBiH came from unemployment contributions. Muamer Halilbašić et al, *Strategija jačanja funkcije posredovanja u javnim službama za zapošljavanje u FBiH* [Strategy for Strengthening the Mediation Function at Public Employment Services in FBiH] (Sarajevo: Economic Institute Sarajevo, Đikić Consulting Services, 2014), p. 33.

³⁸⁸ “Zakon o posredovanju u zapošljavanju i socijalnoj sigurnosti nezaposlenih osoba” [Law on Mediation in Employment and Social Security of Unemployed Persons], *Official Gazette of FBiH* 55/00, 41/01, 22/05, and 9/08, Article 49.

³⁸⁹ *Ibid.*, Article 48.

³⁹⁰ Republika Srpska Employment Institute, “Statut” [Statute], Article 14.

³⁹¹ See Elmira Pašagić, Siniša Marčić and Adis Arapović, *Efficiency of Employment Policies in BiH*, p. 50, Table No. 26.

Table 4.5. Structure of expenditures of public employment institutes in BiH in 2012³⁹²

		Total administration costs	Passive measures	Active measures	Capital investments (and other expenditures)	TOTAL
FBiH	BAM	23.452.935	72.641.834	20.734.356	1.391.435	118.220.560
	%	19,84	61,45	17,54	1,17	
RS	BAM	7.629.546	16.514.945	6.034.813	213.712	30.393.016
	%	25,10	54,34	19,86	0,70	
DB	BAM	624.548	1.160.023	4.374.018	20.751	6.179.340
	%	10,11	18,77	70,79	0,33	
Total in BiH	BAM	31.707.029	90.316.802	31.143.187	1.625.898	154.792.916
	%	20,48	58,35	20,12	1,05	

Source: Pašagić, Marčić and Arapović, 2013.³⁹³

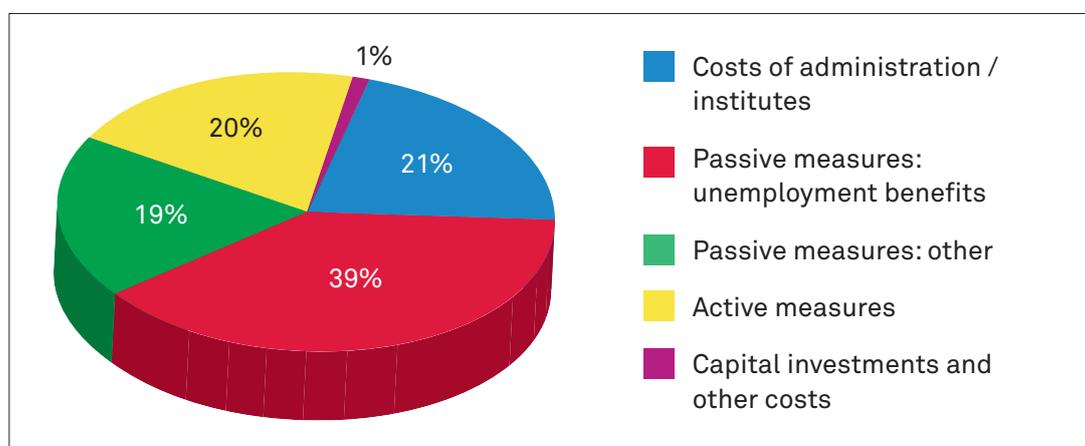
Of the total costs for implementing passive measures, most of the funds in 2012 were used to cover monetary unemployment benefits. Around 63% (45,692,247 BAM) was spent for this purpose in FBiH, around 87% (14,299,985 BAM) in the RS, and 91% (1,054,840 BAM) in BD, out of the total expenditure for passive measures.³⁹⁴ In terms of the structure of aggregate expenditure of employment institutes in BiH, 39.44% (61,047,072 BAM) was spent on benefits (see Graph 4.8).

³⁹² The latest consolidated data on the expenditure of public employment institutes in BiH are available for 2012. It should, therefore, be noted that there is a possibility that the scope of funds spent on individual measures and/or the structure of expenditures has changed over the past three years.

³⁹³ Data according to: Elmira Pašagić, Siniša Marčić and Adis Arapović, *Efficiency of Employment Policies in BiH*.

³⁹⁴ Data according to Ibid.

Graph 4.8. Structure of expenditures of public employment institutes in BiH in 2012



Source: Pašagić, Marčić and Arapović, 2013.³⁹⁵

4.4.4. Unemployment Benefits in Bosnia and Herzegovina

The conditions of entitlement to benefits, the amount and the duration of unemployment benefits in BiH differ among the entities and Brčko District, as shown in Table 4.6 below.³⁹⁶

Table 4.6. Entitlement conditions, level and duration of unemployment benefits in BiH

	Entitlement conditions	Prior employment record ³⁹⁷ / insurance period ³⁹⁸	Duration	Amount
FBiH ³⁹⁹	8 months of continuous employment or 8 months total employment in the past 18 months ⁴⁰⁰	8 months – 5 years	3 months	40% of average net salary in FBiH in the last 3 months prior to termination of employment
		5–10 years	6 months	
		10–15 years	9 months	
		15–25 years	12 months	
		25–30 years	15 months	
		30–35 years	18 months	
		+ 35 years	24 months	

³⁹⁵ Data according to Ibid.

³⁹⁶ Law on Mediation in Employment and Social Security of Unemployed Persons, Articles 29–30.

³⁹⁷ Criteria for FBiH.

³⁹⁸ Criteria for RS and BD.

³⁹⁹ Law on Mediation in Employment and Social Security of Unemployed Persons, Articles 29–30.

⁴⁰⁰ If the person was working reduced working hours, the working hours are converted into full working hours. Ibid, Article 30.

RS ⁴⁰¹	Termination of employment without request, consent or fault of the worker, or termination of self-employment due to economic or technological reasons; ⁴⁰² min. 8 months of continuous employment insurance record in the past 12 months or 12 months with breaks in the past 18 months. ⁴⁰⁴	1–2 years	2 months	35% of average salary earned by the unemployed person in the last 3 months of employment; may not be less than 20% of average net salary, or more than one average net salary in the RS in the previous year. ⁴⁰³
		2–5 years	3 months	
		5–15 years	6 months	
		15–30 years	9 months	40% of average salary earned by the person in the last three months of employment; may not be less than 20% of average net salary, or more than one average net salary ⁴⁰⁵
		+ 30 years	12 months	
BD ⁴⁰⁶	Termination of employment without request, consent or fault of the worker or loss of insurance for other reasons; min. 8 months of continuous employment insurance record in the past 12 months or 12 months with breaks in the past 18 months ⁴⁰⁸ .	up to 5 years	3 months	35% of average salary earned by the person in the last 3 months of employment with up to 10 years of insurance record; may not be less than 20% of average net salary, or more than one average net salary ⁴⁰⁷
		5–15 years	6 months	40% for over 10 years of insurance record; may not be less than 20% of average net salary or more than one average net salary ⁴⁰⁹
		15–25 years	9 months	
		more than 25 years	12 months	

Source: Laws on mediation in employment and rights during unemployment in the RS and FBiH and Law on employment and rights during unemployment in BD

⁴⁰¹ Ibid, Articles 39 and 47.

⁴⁰² Ibid, Article 36, paragraph 3.

⁴⁰³ Ibid, Article 47, paragraph 2.

⁴⁰⁴ “Zakon o posredovanju u zapošljavanju i pravima za vrijeme nezaposlenosti” [Law on Mediation in Employment and Rights during Unemployment], *Official Gazette of Republika Srpska* 72/12, Article 36.

⁴⁰⁵ Ibid, Article 47, paragraph 2.

⁴⁰⁶ Ibid, Articles 30 and 36.

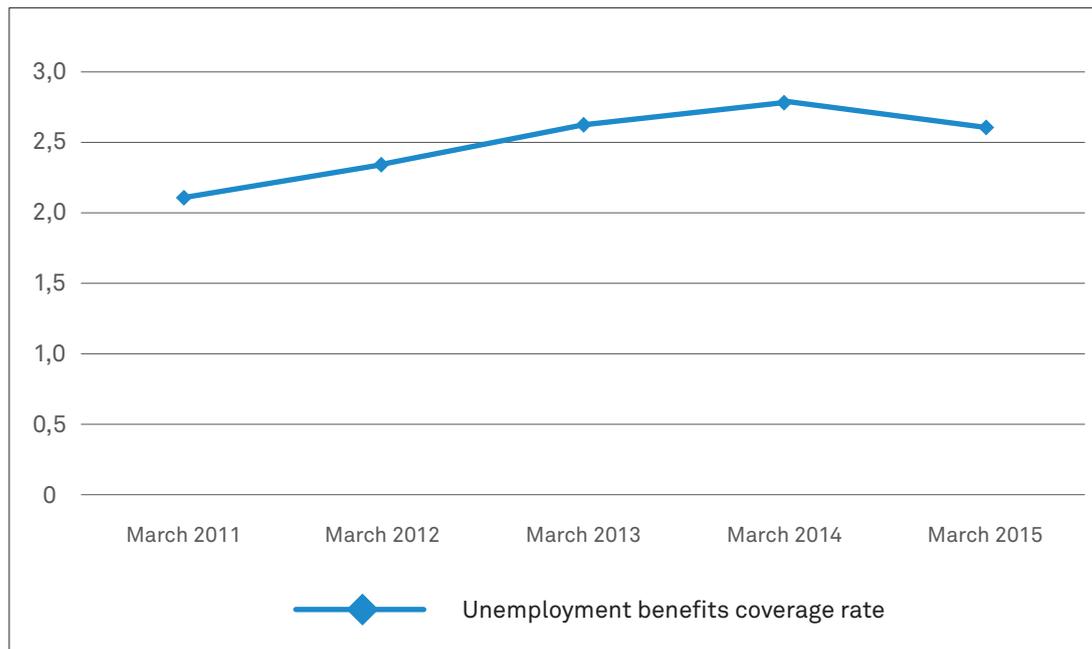
⁴⁰⁷ Ibid.

⁴⁰⁸ “Zakon o zapošljavanju i pravima za vrijeme nezaposlenosti” [Law on Employment and Rights during Unemployment], *Official Gazette of the Brčko District of BiH* 33/04, 19/07,17/08, Article 27.

⁴⁰⁹ Ibid.

Although, as mentioned above, spending on unemployment accounts for almost 40% of total funds allocated to employment policies, only 2.56% of the total number of registered unemployed persons received monetary unemployment benefits in March 2015,⁴¹⁰ which, compared to EU countries, is a very low rate of coverage of job-seekers with this measure.⁴¹¹ It is particularly interesting to note that, compared to March the previous year, the rate of coverage decreased slightly, even though it had exhibited constant growth in the preceding period.

Graph 4.9. Rate of coverage of unemployed persons with monetary benefits



Sources: Calculations by authors based on data from the Agency for Labor and Employment of BiH⁴¹²

⁴¹⁰ The rate of coverage of unemployed persons by monetary benefits is our calculation based on data from the Agency for Labor and Employment of BiH, Statistical Bulletin No. 31 (Sarajevo: Agency for Labor and Employment of BiH, 2014).

⁴¹¹ To provide an example, according to estimates for EU countries for 2010, the average rate of so-called pseudo-coverage (proportion of the unemployed receiving benefits for a period of 3 to 12 months within the total number of unemployed persons aged 18–59) was between 45% and 58% (depending on the duration of benefits). Although data for BiH are not entirely comparable, given that unemployment is measured in line with the ILO methodology (population aged 15+, not 18–59), when compared to the European average, the rate of coverage in BiH of around 2% in March 2011 can be considered extremely low. “Working age poverty: what policies help people finding a job and getting out of poverty,” *Employment and Social Developments in Europe 2013* (Brussels: European Commission, 2014), p. 129.

⁴¹² ALEBiH Statistical Bulletins for the first quarters of 2011–2015, available at: http://www.arz.gov.ba/publikacije/statisticki_informatori/Archive.aspx?langTag=bs-BA&template_id=152&pageIndex=1 (accessed on 17 December, 2015).

Given that unemployment benefits do not guarantee sufficiently wide coverage, and in view of the very low rate of replacement and duration of benefits compared to, for instance, the EU average,⁴¹³ it is fair to say that the unemployment benefits system in BiH does not provide adequate social security to the unemployed and does not have a stabilizing role in the economy. In addition, BiH also lacks unemployment assistance, which is something many European states have. There is a particularly problematic practice in FBiH, where, according to the Centers for Civic Initiatives, the system of benefits in FBiH does not take into account “individual participation in total contributions to the fund, but instead distributes benefits to all in almost the same minimum wage amount [...] and over a relatively long period for certain categories,”⁴¹⁴ so that “this type of benefit is closer in nature to social assistance instead of unemployment benefits.”⁴¹⁵ This is contrary to the previously mentioned practices of a large part of European countries where social security systems guarantee a certain level of income security to persons out of employment, based on their history of contributions to insurance funds.

According to the European Training Foundation, low coverage by the unemployment benefits system in the Western Balkans countries does not provide adequate social security for the majority of the unemployed, thereby exacerbating informal employment practices. Low replacement rates of benefits “constitute a situation of low income security and motivate people to work in the informal economy, even though they are registered as unemployed.” Insurance systems have been weakened by low rates of formal employment, and have been under additional fiscal pressures during the economic crisis.⁴¹⁶

Current reform proposals entirely neglect increasing income security for the unemployed, and therefore fail to recommend improving coverage or increasing the duration or amount of unemployment benefits. This is surprising given the effects that improving income security could have on reducing informal employment. For example, according to the OECD, providing adequately set unemployment benefits or assistance, in combination with effective checks on beneficiaries and their income, can reduce the incidence of low-paid informal employment. In the absence of such benefits, unemployment is not a long-term option and many will have to choose between formal and informal employment. If unemployment benefits reduce the motivation for working in the informal sector, which is simultaneously a measure for reducing poverty, the scope of informal employment will also be reduced, which will in turn make it easier to control. On the other hand, if benefit levels fall below the level of basic subsistence and if control measures against fraud are not put in place or are not effective, such

⁴¹³ Around 60% of net rate of replacement, and benefits duration of at least 6 months.

⁴¹⁴ Centers for Civic Initiatives, *Analysis of Employment Policies in BiH*, p. 45.

⁴¹⁵ Ibid.

⁴¹⁶ ETF, *Activating the Unemployed*, pp. 5 and 3.

assistance can act as an subsidy for informal employment.⁴¹⁷ In any case, it is important to coordinate combating the informal economy through unemployment benefits with other policies, such as employment or making-work-pay policies, in order to ensure the transition to the formal sector.⁴¹⁸

4.4.5. Active Employment Policies in Bosnia and Herzegovina

Although in EU countries, active employment policies play a key role in reducing unemployment, in BiH they are present only in a rudimentary form and mostly concern programs to co-finance employment.⁴¹⁹ In 2012, only 0.09% of GDP was allocated to active employment policies in BiH,⁴²⁰ while, for the sake of comparison, the EU28 allocated an average of 0.45% of GDP to active employment measures in 2011.⁴²¹

⁴¹⁷ OECD, *Employment Outlook 2004*, pp. 228 and 258.

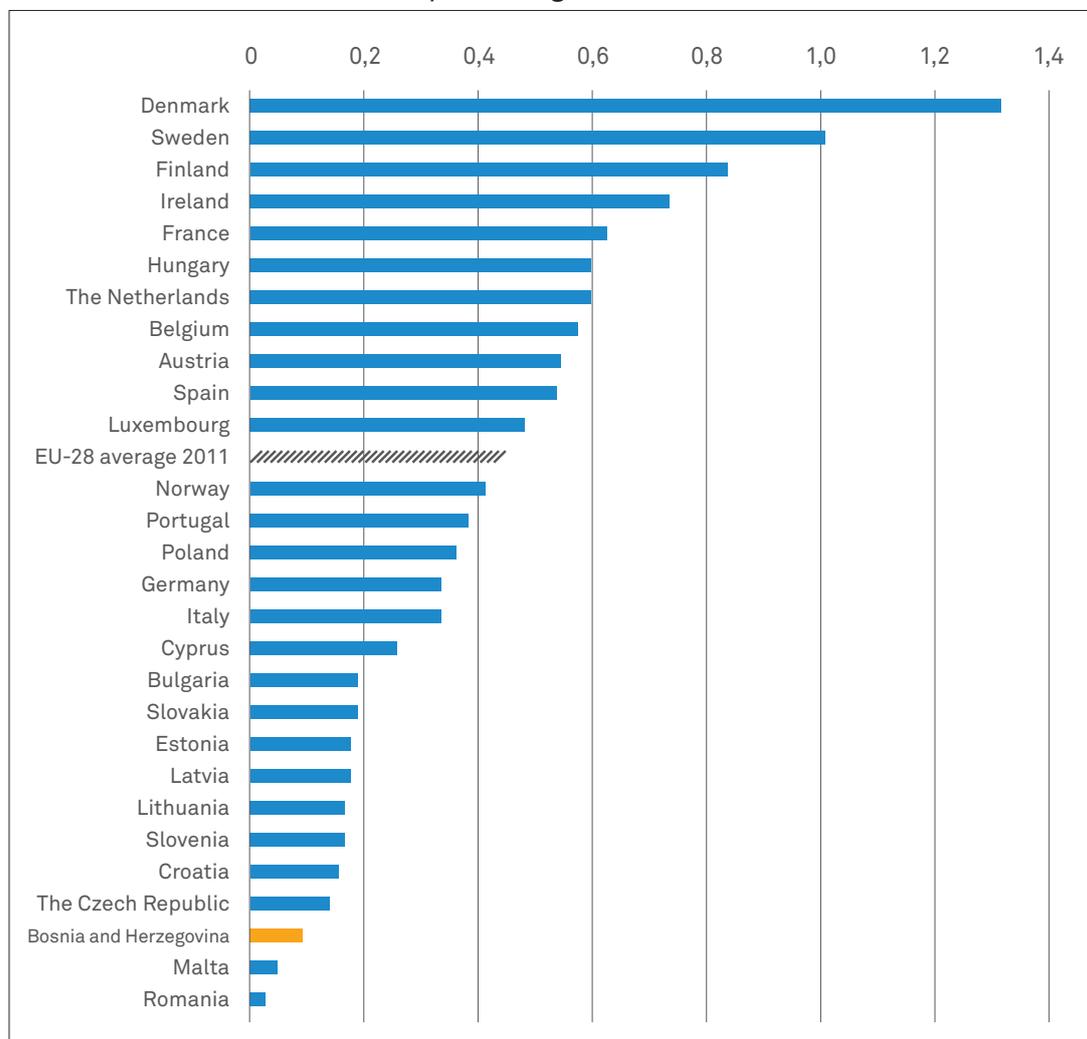
⁴¹⁸ ILO, *Transitioning from the informal to the formal economy*, p. 25.

⁴¹⁹ See Centers for Civic Initiatives, *Analysis of Employment Policies in BiH*, pp. 35–36.

⁴²⁰ Centre of Public Employment Services of Southeast European Countries, *Statistical Bulletin No. 4* (Podgorica: Employment Institute of Montenegro, 2013), p. 44.

⁴²¹ “LMP expenditure: Total LMP measures (categories 2–7),” EUROSTAT, <http://ec.europa.eu/eurostat/web/labour-market/labour-market-policy/database> (accessed on 25 October, 2015).

Graph 4.10. Spending on active employment measures in BiH and the EU28 (except for the UK and Greece, for which data is not available) in 2012 as percentage of GDP



Sources: EUROSTAT⁴²² and Centre of Public Employment Services of Southeast European Countries⁴²³

Furthermore, the data indicates that public financing of employment programs at employment institutes in BiH, in addition to being low, significantly varies from year to year and does not have a tendency of stable growth, while in FBiH in 2012, the amount of expenditure for these programs was considerably lower than in 2007,⁴²⁴ even though unemployment increased significantly in the meantime.

⁴²² Ibid.

⁴²³ Centre of Public Employment Services of Southeast European Countries, Statistical Bulletin No. 4, p. 44.

⁴²⁴ See BiH Directorate for Economic Planning, Bosna i Hercegovina: Izvještaj o razvoju BiH: godišnji izvještaj 2013 [Bosnia and Herzegovina: BiH Development Report: 2013 Annual Report] (Sarajevo: Council of Ministers of BiH, 2014), p. 34.

According to an analysis of the Economic Institute, increased spending on monetary benefits and health insurance between 2009 and 2013 was mostly at the expense of active employment measures, so that allocations for ALMPs were reduced for almost a third.⁴²⁵ This situation is paradoxical in view of the fact that in 2014, around 85% of the unemployed had been looking for work for a year or longer.

In 2012, active employment measures covered 46,644,⁴²⁶ or 8.5%⁴²⁷ of registered unemployed persons, of which a little over two thirds were persons covered by career guidance and counselling services; only 14,403 persons participated in other active employment programs, such as programs for employment, development of entrepreneurship, trainings, professional development, etc. In other words, disregarding career guidance and counselling programs, only 2.6% of unemployed persons were covered by other active employment policy measures, which, along with Macedonia, is the lowest rate of participation in Southeast Europe.⁴²⁸ According to an ILO study on informal employment, there is an evident lack of ALMPs in BiH, and the focus of employment policies focus on wage incentives and self-employment initiatives, which some consider to be expensive and inefficient. On the other hand, measures that are more cost-efficient and effective, such as job counselling and mediation, are not as common.⁴²⁹

Table 4.7. Number of unemployed persons covered by active employment measures in BiH in 2012

Programs and measures	Career guidance and counselling	Additional education and training	Development of entrepreneurship and employment programs	Public works	Employing target groups	TOTAL
Number of persons	32.241	1.056	7.124	-	6.223	46.644

Source: Centre of Public Employment Services of Southeast European Countries, 2013⁴³⁰

⁴²⁵ Halilbašić et al, Strategy for Strengthening the Mediation Function at Public Employment Services in FBiH, p. 35.

⁴²⁶ Centre of Public Employment Services of Southeast European Countries, Statistical Bulletin No. 4, p. 44.

⁴²⁷ Halilbašić et al, Strategy for Strengthening the Mediation Function at Public Employment Services in FBiH, p. 34.

⁴²⁸ Ibid.

⁴²⁹ Cristina Mihes, Natalia Popova and Stefan Roch, *A Comparative Overview of Informal Employment in Albania, Bosnia and Herzegovina, Moldova and Montenegro* (Geneva: ILO, 2011), p. 16.

⁴³⁰ Centre of Public Employment Services of Southeast European Countries, Statistical Bulletin No. 4, p. 44.

In view of the above, it is fair to say that the employment system in BiH is dominated by passive policies that include keeping unemployment records and paying unemployment benefits. In addition, it was found that monitoring and evaluation of the effect of employment policies is underdeveloped, “limiting the possibility for evidence-based policy-making” in this domain.⁴³¹

BiH also suffers from an evident lack of activation strategies that would, for instance, make receiving various benefits contingent on job-search requirements, availability for work or participation in training programs. Given the low demand for labor, these requirements would certainly have to be adapted to the context, but the focus could be on participating in various training programs in order to improve employability, especially for the long-term unemployed. Apart from this, also lacking is a clear link between active employment policies and education policies, as well as professional development, education and lifelong learning, which would shift the focus onto developing the skills needed in various sectors.

Also lacking are strategies to stimulate employment of long-term unemployed or inactive persons, who may also be beneficiaries of various social benefits, but have ability or partial ability for work. Their motivation for employment may be low, given that they are often unable to engage in permanent employment or gain income higher than social benefits, and risk losing these benefits if they accept work, or having their access to benefits, if they lose their job, made more difficult by administrative obstacles.⁴³² At the same time, the inertia of the system is compounded by the limited capacity of employment institutes to devote themselves to these groups, with the outcome being long-term unemployment, benefit dependence and social exclusion.⁴³³ The European Training Foundation has pointed out the importance of various measures to support the poor in sustaining themselves and their families by engaging in work; however, the return to the labor market requires specific approaches depending on the needs of individual social welfare beneficiaries. In some countries, such as Slovenia, improved employment of these groups was achieved through inter-sector coordination between employment institutes, centers for social work, civil society, etc.⁴³⁴

Despite being underdeveloped and not very efficient, the development and improvement of active employment policies in BiH have not received sufficient attention within the previously mentioned reform packages or the Reform

⁴³¹ Western Balkans Investment Framework, “Challenges to successful employment policy in the region – towards more jobs, quality labor force and greater competitiveness,” Discussion paper (2012), p. 9.

⁴³² ETF, *Activating the Unemployed*, pp. 23–24.

⁴³³ *Ibid.*, p. 24.

⁴³⁴ *Ibid.*, pp. 23–24.

Agenda.⁴³⁵ In other words, reform packages focus primarily on the aspect of flexibility, but not the aspect of security (in this case, security of employment), despite the recognized importance of applying active employment measures in the context of long-term unemployment.

⁴³⁵ NERP speaks broadly about the need to improve active employment policies, and the need to define clear objectives/priorities for the use of funds for this purpose in order to ensure they yield the best results. Council of Ministers of BiH, National Economic Reform Programme for 2015, pp. 76, 107. and 119. According to the Reform Agenda, introducing a program of support for first-time job-seekers will be considered. “Reform Agenda for BiH,” p. 5.

5.

Concluding remarks

The BiH labor market faces a host of complex problems: employment is low and unemployment, especially long-term unemployment and youth unemployment, is high; moreover, there is a significant share of persons working in the informal sector. Poor labor market performance can be attributed to factors such as the lack of competitiveness and the unfavorable business environment, as well as the long-term decline in economic activity that results in lower labor demand, an education system not responsive to labor market demands, as well as underdeveloped employment policies that could stimulate job-seeking and improve employability. At the same time, the institutional environment of the labor market is rather weak, with underdeveloped collective bargaining mechanisms, inadequate organization of employment institutes, very limited support in the event of unemployment, and employment policies that cannot respond to the needs of the unemployed and that fail to encourage active job-seeking.

However, it is uncertain to what extent current reform proposals, as well as reforms that are being implemented in BiH, address the causes of poor labor market performance and the shortcomings of its institutional environment. Current reforms mainly focus on deregulation in the realm of employment protection legislation and on restructuring of the tax burden on labor. Flexibilization of working conditions is to be achieved primarily by changing labor laws and collective agreements, while it is not at all certain which aspects of the existing employment protection framework actually prevent hiring and firing of workers in practice and to what extent, or whether or not their impact on labor market performance is significant. Moreover, it also appears that important aspects of employment protection legislation, such as the efficiency of labor dispute resolution mechanisms, have been side-lined. Given the complexity of labor market problems in BiH, making working conditions more flexible will not substantially contribute to resolving labor market problems, especially if other important institutional factors and the interactions between labor market institutions are not taken into account, and if the wider economic environment is disregarded.

When it comes to the tax burden on labor, which is for the most part considered extremely high and has received special attention in current reform proposals, available data shows that the tax wedge in BiH does not deviate from the European average, and the extent to which it discourages employment or encourages work in the informal sector is uncertain. The modalities for restructuring the tax burden have not been specified yet, and it is not clear how they will affect the level of

the tax wedge. In any case, given that current discussions revolve around the option of reducing contributions, especially for healthcare, this requires careful consideration of the implications of such measures for insurance funds. Also, there should be more focus on reducing the tax burden on low wages. Apart from the option of introducing direct progressive taxation of labor, various policies to make work pay should also be considered (e.g. increasing the non-taxable portion of salaries, negative income tax, in-work benefits, etc.) for persons who work, especially for low-income workers and families, but also for unemployed persons and those working in the informal sector as a way to encourage them to transition to the formal sector.

Apart from deregulation in the domain of employment protection legislation and restructuring the tax burden on labor, it seems that other important labor market institutions have largely been neglected. Income and employment security in BiH are very low, and it is paradoxical that they are not being considered in the context of increasing the flexibility of working conditions, given that the BiH market faces low labor demand. Considering that unemployment benefits have a very low replacement rate and limited duration, improvements are certainly needed in order to provide unemployed persons with adequate income security and curtail work in the informal sector. Apart from unemployment insurance, it would be important to consider the option of introducing unemployment assistance as a poverty prevention measure. At the same time, mechanisms to sanction employers in the informal sector should be strengthened, so that benefits do not end up subsidizing informal employment.

Moreover, reforms do not substantially address the extremely weak institutional framework and employment policies, which is precisely what they should focus on given the significant level of long-term unemployment. Currently, unemployment benefits and other forms of support to the unemployed in the form of counselling, training and other employment measures are not the priority when it comes to allocating revenues from unemployment insurance contributions. It would be necessary to increase the financial and human capacities of employment institutes in order to ensure individual counselling for unemployed persons, keep records of vacancies and carry out employment mediation, which are also prerequisites for implementing effective activation policies. The institutional capacities of employment institutes for planning, implementing, monitoring and evaluating employment programs would need to be strengthened in order to enable regular assessment of the efficiency and cost-effectiveness of these programs. It would also be important to strengthen cooperation between employment institutes and centers / services for social work, as well as their cooperation with educational institutions and social partners.

Existing active employment measures are mainly based on co-financing employment. It would be necessary to achieve an adequate combination of training, incentives for employment in the private sector, job mediation services, counselling and progress monitoring, as well as appropriate sanctions for failing to meet any job-search and availability requirements. Programs should

be carefully adapted to various categories of the unemployed and their needs. Given the high degree of structural unemployment, more emphasis should certainly be placed on improving skills and competences, especially for the long-term unemployed, and on harmonizing policies in this realm with the objectives and measures defined in education strategies in BiH. Also, active employment measures should focus on improving career prospects and supporting clients in finding quality employment, so that unemployed persons who participate in employment programs are not forced to accept jobs that offer little in the way of professional development or being lifted out of poverty.

Although collective bargaining mechanisms are considered one of the most important factors for the successful coordination of labor market policies and have proven to be decisive in the implementation of policies that improved labor market performance in numerous European countries, current reform efforts focus on increasing the flexibility of collective agreements without any substantial effort to strengthen collective bargaining mechanisms or social dialogue. In that respect, equal participation of the public and private sector in bargaining mechanisms and social dialogue should be encouraged in order to achieve adequate protection for workers and the representation of the interests of workers and companies in both sectors, and ultimately, to improve collective bargaining mechanisms and social dialogue in order to achieve better coordination and cooperation in designing and implementing complementary reforms in this domain. It will be particularly important to strengthen the capacities of social partners for defining, developing and implementing public policies in the labor market realm and in related policy areas.

In conclusion, comparative experiences indicate that in order to be successful, reforms in this area must be linked to the nature of a country's economy. A significant problem in BiH is certainly the lack of a vision for economic development that the country aims to achieve. For example, if the county's strategy is primarily based on attracting direct foreign investment on the basis of low wages, increased wage flexibility will be at the heart of labor market reforms, but social security must not be neglected in that case. However, if the vision is to improve competitiveness by developing knowledge-based industries, the state should invest in education, research and development and provide incentives for innovation, which is at the heart of the EU Lisbon Agenda, and is not currently the case with reforms in BiH. In other words, without defining a wider framework to improve the labor market, including the development of macroeconomic policies to increase demand and stimulate job creation, improving education and training policies to respond to labor market needs, and improving the institutional environment of the labor market so as to encourage employment and ensure adequate social security for workers, any partial interventions at the level of a few labor market institutions will, at best, have entirely uncertain outcomes.

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