

Reforming non-standard contracts in Slovakia

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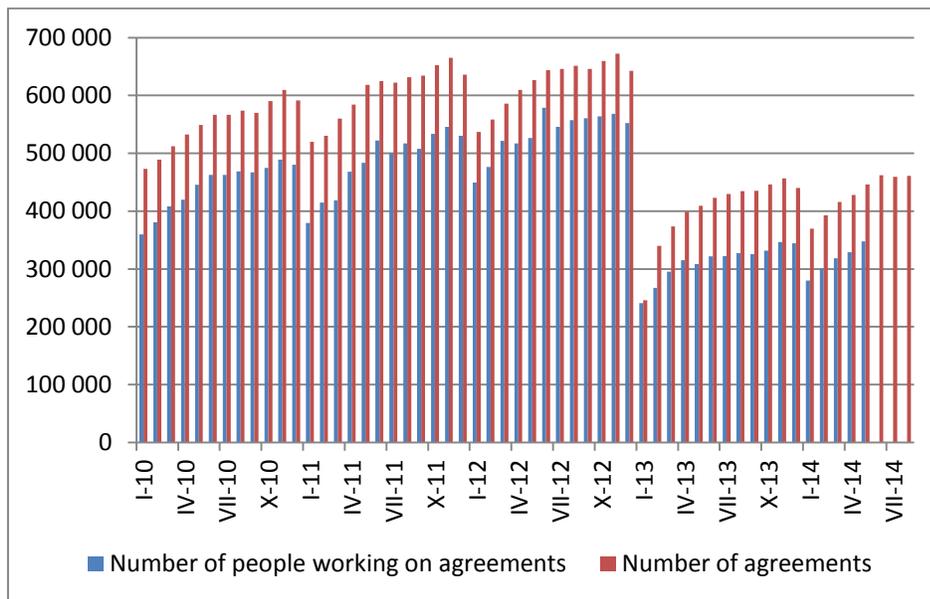
Besides standard employment contracts there are three types of non-standard contracts in Slovakia: (1) agreements to work up to 10 hours per week (40% of all agreements); (2) agreements to perform specific work up to 350 hours in one year (34% of all agreements); and agreements to work up to 20 hours per week for students up to 26 years of age (26% of all agreements). All types of agreements are temporary and may be concluded for a period up to one year. Non-standard contracts are used mainly for small jobs with more than three quarters of people working on agreements earning less than 150 euro monthly which is less than half of the minimum wage of 352 euro in 2014.

The agreements were very popular before 2013 and the firms and individuals started to use them much more intensively especially after the crisis in 2009 apparently in effort to cut the costs. The number of agreement workers increased by around 40% in 2009. Compared to standard employment contracts the agreements offered more flexibility mainly due to relatively easier hiring and firing procedures as well as due to limited regulations protecting agreement workers. For example the minimum wage rule or paid leave rules did not apply to agreements. Moreover the agreements enjoyed much lower tax burden. The social contribution rate of 1.05% was paid on agreements compared to 48.6% rate for standard employment contracts. The personal income tax rate of 19% was the same for agreements and the standard employment contracts; however, this rate was applied only from the income above 304 euro monthly in 2013 (raised to 317 euro in 2014). The massive use of agreements highlighted several problems such as the limited protection of workers who were not entitled to social benefits such as social security, unemployment benefits, paid sickness leave, etc. Another problem was the tax evasion.

As a reaction the government adopted a reform in 2013 increasing social and health contributions to the same level as for employment contracts, e.g. from 1.05% to 48.6% of the gross income paid by both workers and employers. There remained several exceptions, here are the most important of them: (1) Service and old-age pensioners pay a reduced rate of 23.8%; (2) disability pensioners and students pay a reduced rate of 29.8%; (3) students up to 18 years of age pay 1.05% from income up to 66 euro monthly; and (4) students up to 26 years of age pay 1.05% from income up to 155 euro monthly (from 2014 there will be a single 200 euro threshold for all students up to 26 years of age). The government also applied minimum wage rule to all agreements.

The reform coming into effect from January 1st, 2013 had immediate impacts. The number of people working on agreements decreased by almost 60% in January 2013 compared to December 2012. Later the decline retreated a bit and the year-on-year decrease was almost 40% in December 2013 corresponding to a reduction from 552 thousand in December 2012 to 344 thousand in December 2013.

Number of agreements and people working of agreements



Source: INEKO based on data from the Social Insurance Agency

What happened to people who ceased to work on agreements? There was no significant change in the number of employees (1.96 million both in 4Q 2012 and 4Q 2013), registered unemployed (0.39 million both in 4Q 2012 and 4Q 2013) and self-employed (0.36 million both in December 2012 and December 2013). Partial answer gives a detailed structure of those who cancelled the agreement. Particularly, there were 111 thousand less people working both on the agreement and on the standard employment contract or as self-employed in December 2013 compared to December 2012. The net income of people who ceased their agreement and continued working on standard contracts decreased on average by more than 60 euro monthly (Source: [INESS, 2013](#)). What happened to remaining 97 thousand? We do not have specific data but we can assume that some of them are pensioners and probably most of them moved to the shadow economy.

In a survey among 25 firms employing 15-thousand people (Source: [Adecco](#), July 2013) two thirds of firms reported they had to react to the changes applied to agreements. From those impacted three out of four firms restricted agreement contracts, one in four changed agreements for personal leasing, 22% changed the organization of work, 22% reacted by firing people, 16% reported decreased profits, 16% increased prices of their products and just 4% reported they changed agreements for the standard employment contracts.

The downside of the reform was that it transferred the full payroll-tax burden on people regardless of their income (with above mentioned exceptions). This caused a rapid decrease in their net income and forced part of them to escape to the shadow economy. In particular people with labor productivity below minimum wage have been hit hard. After applying minimum wage to agreements they in fact lost possibility to work legally. The problem is even more important in Slovakia where around 8% of total population is from Roma minority with typically low qualification and thus unable to find a well-paid job.

As a result the Roma are assumed to represent around one third of registered unemployed. The registered unemployment rate was at 13.5% in December 2013.

To solve the problem of high unemployment of low-skilled people INEKO proposed in 2013 to decrease social and health contributions for people with low income. The proposal took inspiration from the German mini and midijobs. INEKO presented three alternatives. All people working on agreements and/or employment contracts should be freed from paying social and health contributions from their total income up to a certain threshold (in one alternative it was 2/3 of minimum wage) and pay gradually higher contributions from higher income and full contributions from the upper threshold (4/3 of minimum wage for this alternative). The state should pay for the missing contributions. The Institute for Financial Policy at the Ministry of Finance of the SR calculated the public finance impact of all three alternatives ranging from 79 million euro in 2015 for the mildest alternative to 749 million euro for the boldest one.

In 2014 the Ministry of Finance presented its own proposal known as a health insurance allowance. The employment contracts (i.e. not agreements) with income equal to a new minimum wage of 380 euro monthly would be freed from paying health insurance contributions. The effective rate would increase linearly with higher income and the full 14% rate would be paid from a certain threshold (e.g. minimum wage multiplied by 1.3). This is similar to INEKO proposal but there are several distinctions: (1) Different thresholds; (2) rapid increase in minimum wage; (3) the allowance does not apply to agreements only to standard employment contracts; (4) the allowance does not include the social contribution rate which remains at 34.6% of the gross income. The ministerial proposal should come into effect from 2015. It is assumed to increase net income of around 0.5 million people and cost around 150 million euro in 2015. The goal is to increase motivation to work for low wages and thus to help to decrease unemployment.