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III. Issues in fostering labour force participation and employment

Reducing barriers to labour force participation is crucial for raising Austria's growth performance and increasing the capacity of the economy to respond to future challenges, notably in terms of a rapidly ageing society. This chapter considers major issues in this respect, such as policies associated with the recent pension reform and matters relating to female labour force participation. Equally important, a number of specific issues need to be addressed to ensure that labour demand meets supply. In particular, wages need to be sufficiently flexible to adjust to productivity, and non-wage labour cost needs to be reduced. Finally, education and training is increasingly important in a knowledge based society to safeguard high employment levels and boost productivity. There appears to be considerable scope to improve the efficiency of Austria's education system, major aspects of which are considered in the last part of this chapter. A summary of present and earlier recommendations is contained in Box 4 at the end of the chapter.

Reducing hurdles to labour force participation

Pensions

Austria's public pension system encouraged early retirement and discouraged higher labour supply over the life cycle more generally. The system is also fiscally costly. Recognising the threat of demographic developments to the fiscal sustainability of the system, consecutive governments implemented pension reforms for the general scheme for workers and salaried employees (ASVG) in 1993, 1997 and again in 2000. Although containing important elements, these reforms remained partial. Without further action the system was set to come under stress, and steeply rising pension contribution rates would have increased non-wage labour costs with adverse effects on employment. Simulations made by the Pension Reform Committee, appointed by the federal government, indicated that without further reform pension outlays, net of those for civil servants, would increase from 10½ per cent of GDP in 2000 to between 14.2 and 15.6 per cent in 2035, depending on assumed employment rates.³⁶ Against this background, the

government has tabled a far reaching reform, which was adopted by Parliament in June 2003 (see Box 3). The reform marks substantial progress in securing the sustainability of general government finances. Some important elements are still missing, however, and need to be implemented soon.

A key element of the reform is the phased increase – until 2028 – in the number of years that count for the wage base of the pension claim (*Durchrechnungszeitraum*) from the current best 15 years (18 years in case of early retirement) to 40 years. The former regulation favours employees with minimal employment contracts beyond the “best” 15 years relative to those with more steady (full-time) employment. The latter pay *ceteris paribus* greater pension contributions over their life time than the former while both groups receive the same level of pensions. This discourages labour supply over the life cycle. In addition there is an incentive to maximise pension claims by pushing up wages with seniority, with potentially negative implications for the firms’ labour demand for older employees. Basing the level of pensions on 40 years of earnings largely removes these distortions. Moreover, strengthening the link between contributions paid and benefits received allows employees to consider their contributions as savings rather than a tax, improving the base for their saving and consumption decisions. The reduction in the annual accrual rate for pension claims reduces incentives to retire early.³⁷ Both measures combined imply that for a given length of a person’s work history replacement rates will be lower than prior to the reform, the more so the more variable the shape of the earnings curve over the life cycle.

Likewise key is the ending of early retirement on account of unemployment, and the introduction of larger discounts for early retirement on account of long insurance histories. Up to now retirement prior to the statutory retirement age has been the rule rather than the exception (see Figure 8 above). As has been argued in previous *Economic Surveys*, income replacement for the unemployed should be dealt with within the unemployment insurance and placement system rather than within the pension system. This preserves incentives to stay in the labour market, while early retirement represents workers dropping out of the labour force and is hard to reverse. Maintaining labour force participation, in turn, can increase the pressure to set wages and employment conditions in a way that accommodates re-employment. Overall, closing the channels into early retirement under preferential conditions is vital to relieving the general government budget and reducing the cost of inactivity to society more generally.

With such reform, care needs to be taken that no other channels into early retirement act as substitutes for those that are being closed. Previous *Surveys* on Austria found that inflow into other types of early retirement increased when eligibility conditions for one particular channel were tightened. While the previous pension reform in 2000 has reduced the scope for this type of substitution by abolishing early retirement on account of disability within the old age pension

Box 3. Pension reform 2003

Parameters of Austria's general public pension scheme for workers and salaried employees (ASVG)

Within the ASVG the size of a pension for the transition year into retirement is determined as follows

$$B = W * (S + A) \text{ with}$$

B = Level of monthly pension;

W = Pension base: average – revalued – monthly earnings over the past 15 years of highest earnings (in case of early retirement: period extended up to the best 18 years);

S = Sum of annual percentage point accruals per year of insured work history, added over 40 years (*Steigerungsbetrag*);

A = Deduction (premium) for every year of earlier (later) retirement than the statutory retirement age; A is negative with early retirement and positive otherwise (*Abschlagsfaktor* or *Zuschlagsfaktor*).

Earnings in the wage base (W) are revalued by a pension adjustment index (*Aufwertungszahl*) so as to express earnings in terms of constant prices. Child care periods without employment increase W by a fixed monthly amount (€ 640 in 2003), for a maximum period of four years per child. In the accruals sum (S) 12 insured months (including qualifying periods) account for 2 percentage points. The accruals sum is reduced by a deduction (A) of three accrual points per year retired earlier than the statutory retirement age (65 and 60 years for males and females, respectively). The maximum replacement rate is 80 per cent of past real wages (W) after an insurance history of 40 years or more. The maximum deduction (A) amounts to 10.5 accrual points or 15 per cent of all accrual points. For each year of later retirement over the regular age S is increased by a premium of 4 percentage points. When a premium is granted the maximum replacement rate is 90 per cent, instead of 80 per cent, of the pension base. Once retired, current pensions are adjusted annually. The size of adjustment is decided by a commission – comprising the social partners, the Ministry of Social Security, Generations and Consumer Protection, the Ministry of Finance, the political parties represented in Parliament, and economic research institutes (*Kommission zur langfristigen Pensionsicherung*) – and has kept pensions growing moderately in real terms.

Pension reform measures

The government's pension reform bill (*Pensionssicherungsreform 2003*), initially faced stiff opposition in the public policy debate. In the process, some provisions were softened. The law came into force in August, and contains the following major elements:

- The accounting period (*Durchrechnungszeitraum*) for the pension base (W) will be gradually increased to the best 40 years of earnings for which contributions were paid (instead of the best 15 years). The extension is phased, with 12 months annually, starting in 2004 and finalised in 2028. The crediting of child care periods in the pension base (W) will rise from € 640 by 50 per cent in 25 years. Times for caring for dying relatives or seriously ill children are taken into consideration in the accruals period (*Familienhospiz*).

Box 3. Pension reform 2003 (cont.)

- The annual accrual rate (contained in S) will be reduced to 1.78 per cent (instead of 2 per cent), so that the full replacement rate of 80 per cent of past real wages (W) will be reached after an insurance history of 45 years or more (instead of 40 years).
- Early retirement on account of unemployment will be abolished.
- The minimum age (61.5 for men and 56.5 for women) for early retirement on account of long-term insurance contributions (35 contribution years for both men and women) will be increased in steps until 2017 to the statutory retirement age of 65 for men and 60 for women. Within the transition period, the deduction (A) for every year of earlier retirement will be increased to 4.2 per cent (instead of 3 per cent), up to a maximum of 15 per cent of the pension.
- The premium for later retirement will be increased by the same amount, up to a maximum of 10 per cent.
- Starting in 2004, maximum losses implied by the transition to the new system are capped such that they cannot exceed 10 per cent at the maximum.

Regarding the pensions of tenured civil servants the bill foresees the following steps:

- Extension of the pension base to 40 years (instead of the last salary). The transition period will last until 2028.
- A reduction in the annual accrual rate.
- Stepwise increase in the retirement age to 65 years.
- For civil servants with long-term tenure, early retirement at age 61.5 is only possible with discount.
- Increase of pension contributions by 1 percentage point.
- Increase of the percentage deduction for early retirement from 3 to 3.36 per cent.

system, there is still a risk that the invalidity retirement scheme outside the old-age pension system could act in a similar way. To avoid this, it needs to be ensured that eligibility conditions within the invalidity scheme are strictly conditional on health reasons only and tightly controlled. Moreover, there should be regular follow-up checks of health conditions, and re-entry into the labour force should be required if the degree of invalidity improves sufficiently. Several countries within the OECD follow this standard.³⁸ Other channels into effective early retirement outside the pension system also should be closed (see further below).

The increase in the actuarial adjustment factors for early retirement on account of long insurance spells is a welcome move towards actuarial fairness. This

points to an important option for further developing the public pension system after the present phase of reform. There is no need to restrict retirement to a certain age or contribution period. Instead, a high degree of flexibility in the individual retirement decision could be secured if pension benefits were adjusted such that the expected discounted value of pension income at retirement would not increase with earlier retirement once a minimum pension level is achieved. Actuarially fair adjustment of pension claims would in principle allow employees to determine the length of their working life taking into consideration the trade-off between shorter life-time employment and lower pensions, while securing that early retirement would not raise the fiscal burden for the pension system. Policy makers could define financially viable replacement rates for a certain reference contribution period (such as 45 years), and deviations in both directions of actual contribution periods from the reference period would be associated with the actuarial reductions or bonuses. In practice, widening the choice to employees along this line also requires that the system is set up in a way that allows the insured to identify their claims, given their elapsed employment and contribution histories. This would be facilitated by establishing individual retirement accounts, which would also remove the distortions of the current system in favour of steeper earnings curves over the employment history. The government has expressed the intention to introduce such accounts in the next phase of reform. This should be implemented and associated with actuarially fair adjustment.

Introducing individual retirement accounts would tend to move the system toward a defined contribution system, although it still might have defined benefit elements. Benefits that are unrelated to individual contributions by the recipients are best financed out of general tax revenues rather than wage-based contributions. Hence, the size of redistribution – such as minimum pensions – should be identified and tax financed, to the extent the redistribution is not yet covered by transfers out of the federal budget, in order to promote actuarial fairness and tackle Austria's high level of non-wage labour costs.

Harmonisation across Austria's different public pension schemes is still to be achieved. As has been outlined in Chapter II above, harmonisation of the pension schemes for civil servants with the general pension system for workers and salaried employees (ASVG) should be an important part of public sector reform. While the pension reform law contains adjustments of the system for federal civil servants, harmonisation is not complete yet. The pension systems for the civil servants of the states are not included in the reform and remain dispersed. Apart from the ASVG, which represents the largest part of Austria's public pension system, there are also branches for special occupational groups such as notaries, self-employed and farmers. At present the responsibility for administering the different insurance schemes is split accordingly. This fragmentation is non-transparent and provides incentives to pressure groups to lobby for more favourable benefits – involving state subsidies – for their respective clienteles. Setting the same stan-

dards across the different branches of the public pension system is important to improve the efficiency of labour allocation in the economy overall.

Strengthening the funded layer of the pension system

In the public debate surrounding the design of the present reform, transition periods to the revised system have been criticised as too short. However, stretching out the adjustment of the pension parameters too far into the future would increase the upward pressure on contribution rates and shift the fiscal burden to the next generation while reducing incentives to adapt private saving plans. In fact, this is similarly true for the capping of losses that has been legislated over a transitory period. However, efforts need to be made to ensure that efficient instruments are available to support private retirement savings as a supplement to the pay-as-you-go part.

The almost universal coverage of public pensions in combination with income replacement ratios that are high by international comparison have implied that private pension savings are among the lowest in the OECD. In January 2003 a new private pension scheme was introduced that is associated with a tax preference (*Zukunftsvorsorge*). The scheme not only aims to promote private pension provisions but also the Austrian capital market. To this end, the scheme requires that at least 40 per cent of the funds' capital needs to be invested in European countries with a low stock market capitalisation.³⁹ However, restraining the diversification of pension investments across developed capital markets could increase the risks of Austrian pension fund portfolios. In the same vein, it is conceivable that a boost in the supply of funds would not be readily absorbed by the narrow Austrian market. In the longer run, the provision could also restrain the funds' potential returns and make it more costly to meet the additional requirement that the savers' contributions be guaranteed in nominal terms. Hence, the thin-market provision should be dropped, and broader diversification of portfolios should be allowed as in other countries with large retirement savings. Regulation should allow for maximum returns on assets while at the same time minimising the risks for the long-term solvency of the funds.⁴⁰

The last *Survey* highlighted the adverse implications of Austria's severance pay system for labour market flexibility and described the plans to turn the system into a tool supporting the development of funded company pensions. Meanwhile, the system underwent thorough reform. In the new system (*Abfertigung neu*), which became effective in January 2003, the management of severance pay is attributed to retirement accounts, which are legally independent from the employers (*Mitarbeitervorsorgekassen*) and funded by employers via a monthly untaxed payment of some 1.5 per cent of gross wages. Accumulated entitlements rest in the employee's account until retirement, unless the work contract has been terminated by the employer, which makes cash payments admissible under cer-

tain conditions. Upon retirement, employees can either claim a cash payment or convert their entitlement into an annuity. While the former is taxed at a rate of 6 per cent, annuities remain untaxed. Investment rules under this regime are the same as they are for pension and life insurance funds.⁴¹

Several features of the revised system make it suitable to strengthen the funded pillar of the pension system. In contrast to the former system, entitlements now commence almost immediately (after one month of employment) and are portable across employers. Moreover, eligibility is extended to almost all employees by including the cases where contracts are terminated by the employees, and allowing seasonal workers to accumulate entitlements. These features combined extend employer based savings schemes to the vast majority of employees, independent of their occupation and length of employment spells. Moreover the reallocation of funds via the capital market – rather than the retaining of funds that was widely applied under the predecessor scheme – should improve the role of the capital market in supporting growth. On the other hand, the fact that employees are forced into savings reinforces the need to encourage competition among providers while minimising the risks of insolvency.

Old-age part-time employment and unemployment benefits

As outlined in Chapter I, the old-age part-time scheme (*Altersteilzeit*) has failed to deliver increased hiring of younger people, and has opened a highly utilised and fiscally expensive channel into early retirement outside the statutory old age pension system.⁴² While early retirement fell steeply in 2001, when the disability scheme was abolished, inflow into *Altersteilzeit* surged, pointing to a certain degree of substitution between both schemes (see Figure 8 above). This undermines policies to raise the effective retirement age. Accordingly, the government revisited the scheme. From 2004 onwards working full-time during the first years covered by the scheme and ceasing work entirely in the remainder of this period will only be possible if another part-time employee is recruited. Also, financial support is halved without a new recruitment. This change makes it more difficult to enter “full-time” early retirement. However, the reform preserves financial incentives for those who have worked full-time to cut down their number of hours worked. This adverse labour supply effect might also strengthen resistance to reform of seniority wage schedules that would be conducive to higher labour demand. Hence, it should be considered to abolish the *Altersteilzeit* scheme entirely.

Unemployed aged 60 and older enjoy an extended eligibility period for unemployment insurance benefits of 78 weeks (subject to a certain contribution period). This preference, which has been introduced in 2001, is set to expire at the end of 2003. However, new legislation lifts unemployment benefits by 25 per cent for older persons so as to grandfather the termination or phasing out, respectively,

+of early retirement. For similar reasons, this measure should be phased out so that incentives for job search are increased and extending a road into factual early retirement is avoided.⁴³

Family support

Family friendly support policies rank high on the government's agenda. Within the OECD Austria is in the top range with respect to resources devoted to child care.⁴⁴ In 2002 child care benefits were extended substantially (*Kinderbetreuungsgeld*, KB). The goal was to extend the duration of the benefits by one year so as to widen the parents' choice with respect to the utilisation of child care and make it easier for women to reconcile work and family obligations. As has been argued in the last *Survey*, the impact of the new scheme on female labour force participation is ambiguous *a priori*. On the one hand, higher tax-free earnings allowances raise incentives to expand part-time work. On the other hand, the income effect associated with higher benefits and the extension of the eligibility period tends to reduce labour supply. Prolonged spells of non-participation are likely to make it more difficult from the labour demand side to re-integrate parents into the labour market because of a more profound depreciation of their skills. First empirical evidence suggests that on balance the new scheme might diminish female labour supply by reducing re-entry rates into employment.⁴⁵ It is too early, however, to arrive at comprehensive empirical conclusions. The government has therefore commissioned a study to evaluate the impact of the regime shift on labour market responses.

The majority of childcare benefit claimants is on parental leave, and therefore only entitled to earn up to 15 per cent of the earnings of an "average production employee" (APE), unless their employer agrees otherwise. Alternatively, if the parent gives up employment protection child care benefits are paid up to a ceiling of 69 per cent of APE earnings. If earnings rise above this level, the benefits are not gradually phased out but withdrawn completely. This produces very high marginal effective tax rates providing strong disincentives to expand earnings above the threshold value. Overall, in this case, a second earner with average earnings faces an effective tax rate of 52 per cent, up from a level of some 25 per cent when the parent earns two third APE (Table 10). Hence, the parameters of the system should be reconsidered so as to remove disincentives for labour force participation. One option would be to introduce a part-time work entitlement for parents on parental leave. Moreover, a phased reduction of the child care benefits would reduce marginal effective taxation of earnings.

Fixed costs of work, both monetary and non-monetary, have often been found to be an important impediment to female labour force participation. Fees to be paid for using a child care facility as well as commuting times to reach the facility are arguably the most important monetary and non-monetary fixed costs,

Table 10. Taxes and benefits for couples with children

Wage level (first adult – second adult) in per cent of the earnings of an APE	100-0	100-33	100-67	100-100
	Euro			
1. Gross earnings ¹	23 963	31 550	39 938	47 926
	Per cent			
Transfers (relative to gross earnings)				
2. Payments to government				
Income tax	9.0	7.6	8.1	10.6
Social security contributions ²	18.1	18.1	18.1	18.1
3. Family benefits from government				
Children aged 1 and 4	38.1	28.6	22.9	8.1
Children aged 7 and 9	16.3	12.2	9.8	8.1
4. Total payments to government less family benefits (2-3)				
Children aged 1 and 4	-11.0	-3.0	3.3	20.5
Children aged 7 and 9	10.8	13.4	16.4	20.5
5. Average effective tax rates on second earners ³				
Children aged 1 and 4		20.4	25.1	52.0
Children aged 7 and 9		20.4	25.1	30.1

1. APE or "average earnings" refer to the annual earnings of an Average Production Employee (APE) in the manufacturing sector. In 2002, these were \$23 963 (€ 22 543) in Austria.

2. At the example earnings levels Austrian individuals are below the ceiling for social security contributions (164 per cent).

3. Average effective tax rates are calculated as the difference between the increase in gross earnings, and the increase in net income when a second earner starts work on 33 or 67 per cent of APE, expressed as a proportion of the change in gross earnings.

Source: OECD (2003), *Review of Family Friendly Policies in Austria, Ireland and Japan*, Paris, forthcoming.

respectively, associated with child care. In Austria child-care costs reduce the financial returns to second earners substantially, despite quite generous (means-tested) subsidies for child-care facilities.⁴⁶ In line with this observation, for both children aged up to three years and at school age utilisation of childcare facilities is low, standing at 13 per cent for both groups.⁴⁷ At the same time, there is a substantial excess demand for child-care facilities for children of the same age groups.⁴⁸ The KB does not lower the fixed costs of work, since it is granted unconditionally. Hence, one way to improve the compatibility of work and family obligations would be to devote a larger share of total family benefits in favour of child-care facilities so as to increase capacities and cut commuting times.⁴⁹ Giving financial support to the users rather than providers of services would help to improve the efficiency of the child care sector. Reallocating some part of the resources along this line would also help reducing marginal effective tax rates associated with benefit withdrawal when eligibility for KB is exhausted. Moreover, an option to reduce the supply constraints of care for children at school age would be to offer more opportunities

for full-day schooling. At present, half-day schooling is the rule in Austria, with the supply of full-day schools being very limited, although progress has been made with respect to all-day supervision at schools.

In the same vein, regulatory issues of labour and product markets also come into play – and often interact – when it comes to reducing the costs of labour force participation of parents with small children. For example, combining child raising and labour-force participation would be facilitated if shop opening hours were further extended. Moreover, the decision on home production *versus* labour-force participation is influenced by the ease with which certain goods or services are available at competitive prices. A large variety of processed food, or a flexible retail system that allows deliveries of products at home as an option stand as examples. In contrast to income transfers, such regulatory measures do not burden government budgets and are beneficial for the economy overall. This reinforces the case that Austria should step up regulatory reform of the type highlighted in Chapter IV below.

Reducing the costs of employment

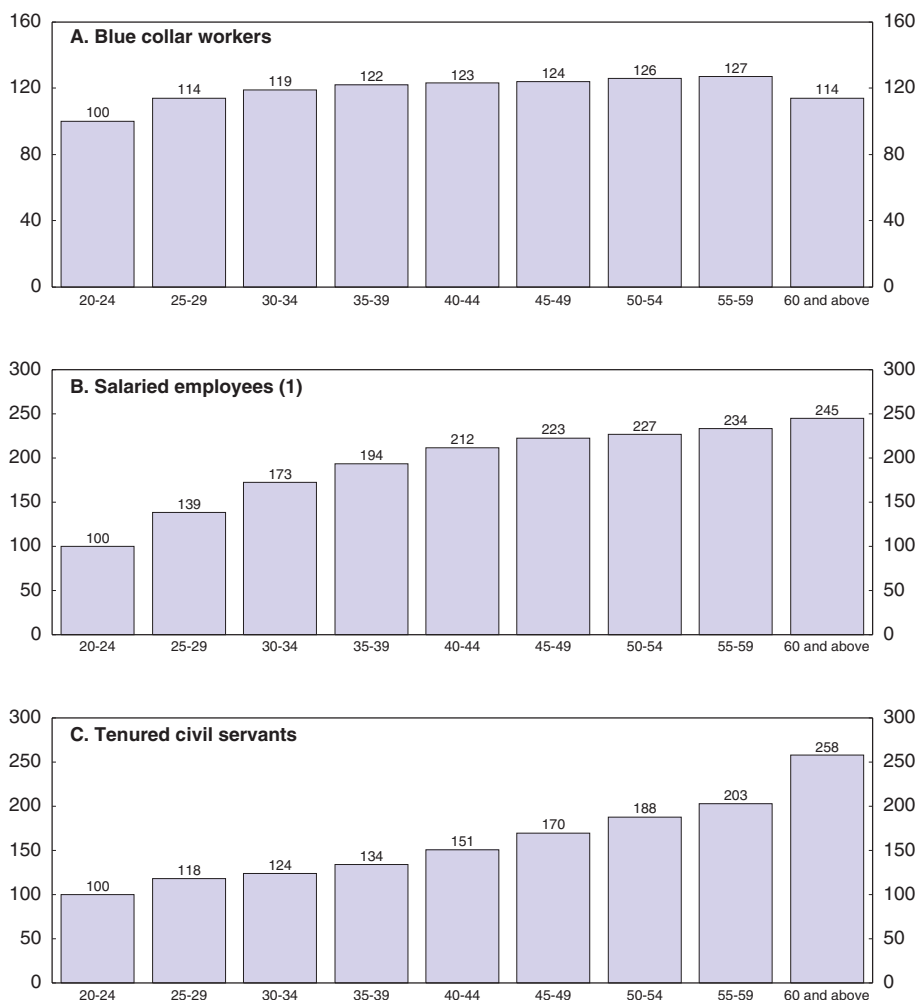
Increasing wage flexibility

Empirical work indicates that real wage flexibility at the macro level is high in Austria.⁵⁰ This has helped the economy to accommodate demand fluctuations over the business cycle while avoiding large fluctuations in unemployment. However, both the adaptability of the economy to relative shocks and the employability of certain groups of employees, such as older people, require that relative wages can adjust to asymmetric forces. Several factors indicate that the flexibility of relative wages in Austria on the disaggregated level needs to be improved to increase the adaptability of the labour market to globalisation and technological shocks.

Wages need to adapt better to the age profile of productivity...

Wages in Austria rise significantly with age for both salaried employees and civil servants independent of the productivity level. This is particularly pronounced in the government sector, where per capita wages of employees aged 60 and over exceed the wages of the 55 to 59 year old group by 27 per cent (Figure 15). For both tenured civil servants and salaried employees in the private sector, wage profiles by age are shaped by automatic biannual salary steps that are fixed by ordinance or in collective contracts, respectively.⁵¹ By contrast, in nearly all other OECD countries wage profiles appear to be either less steep or decline in the older-age brackets.⁵² To some extent, especially in a structurally stable environment, seniority based wage increases might reflect productivity gains due to experience or support the creation of internal labour markets. However,

Figure 15. **Wage-age profiles for men, 2001**
Age group 20-24 = 100



1. Excludes tenured civil servants.

Source: Statistics Austria.

observed wage schedules in Austria are likely to be biased upward, against higher labour demand for older people. As is well known, regulatory features of labour and product markets can effectively insulate wage setting for certain groups of employees from underlying market pressure. In Austria, tighter dismissal protec-

tion for older employees who already have a job, early retirement programmes, subsidised old-age part-time employment and extended unemployment benefit periods for older unemployed are all such insulating factors. Moreover, the fact that the level of pensions is determined on the base of the last earnings in the government sector, or the best earnings within the last 15 years of a person's employment history in the private sector, adds to incentives to push up wages with seniority. Also, as far as the salaried employees in the private sector are concerned, both some degree of substitutability of employment between the government and the private sectors and equity considerations are likely to support a certain spill over of high administratively fixed wage steps from the government sector into the private one. These factors combined might also have adverse implications for the mobility of older employees, in that a change of employer can lead to a partial loss in seniority based remuneration.

To lower labour costs and raise the employability of older people when early retirements are being curbed via the recent pension reform, the government plans introducing a training programme targeted at older workers and to reduce social security charges for older employees (see Chapter II above). Notwithstanding the fact that high non-wage costs have adverse effects on employment, subsidies for this end need to be judged with caution. Indeed, there is a risk that financial support could be counter productive by just adding to the factors that insulate wage setting from imbalances on the labour market. Instead, policies should aim at abolishing the factors that hold wages for older people artificially high. Several recent policy initiatives, such as the extension of the wage base for pension claims, already go a considerable way in this direction. Further reform is necessary, such as revisiting remuneration schemes in the public sector (see Chapter II above). Moreover, the social partners should revise the present system of seniority based remuneration. While some adjustment was made in the past, it remains insufficient. Rebalancing the system in line with demand and supply conditions should not stop short of cuts in relative pay so as to support higher labour demand for older people.

... and to shocks hitting the sectors and companies asymmetrically

Increasing the growth potential of the Austrian economy requires that labour markets are sufficiently flexible so as to support labour reallocations in line with market signals. Empirical evidence suggests that in Austria the distribution of relative wages across sectors is relatively unresponsive to shifts in demand and supply.⁵³ In the same vein, wage determination appears to have rigid elements when it comes to wage differentiation at the firm level.⁵⁴ Collective contracts for about one-third of employees, mainly in the manufacturing sector, determine actual wage increases rather than minimum wages. To give firms some discretion for differentiated wage increases that deviate from such collective agreements,

optional “redistribution clauses” were introduced from 1997 on into several collective contracts (*Verteiloption*, VO). Typically, VOs allow some wage differentiation within the firm’s workforce, provided there is an agreement between the firm’s management and the workforce, and subject to further conditions concerning the total wage bill. For example, the collective agreement for the metal industry of autumn 2002 determines wage increases of 2.2 per cent. The contract’s VO allows wage differentiation, provided the minimum increase is 1.9 per cent, and in addition the total wage bill rises by at least 2.5 per cent.

Hence, VOs are exclusively designed for the purpose of income redistribution within a firm’s workforce but preclude adjustment of wages in accordance with differential developments in employment conditions and productivity. Quite in contrast, exercising a VO would often raise a firm’s total wage bill by more than uniform pay increases, as is the case in the metal industry. Moreover, application of VOs might be hampered by conflicting goals of employers and work councils. For the former, the instrument might be potentially useful to support performance-oriented pay differentiation. By contrast, work councils might be more interested in equalising the wage distribution within the firm, in accordance with a tendency in aggregate collective bargaining outcomes. Accommodating conflicting distributional goals might be costly, however, reducing the attractiveness of VOs for employers further. Not surprisingly, VOs appear to be rarely used in practice, with polls among managers pointing to higher costs and administrative burdens as well as potential frictions within the workforce as main reasons for low utilisation.⁵⁵

Overall, much more should be done to increase the responsiveness of wage setting to market forces. In particular, the VOs should be developed into opening clauses that allow firms to deviate from collectively bargained outcomes in both directions if a plant level agreement comes about between the firm’s management and the labour force. Without such agreement collectively agreed outcomes would remain the default.

Revisiting employment protection

OECD indicators, referring to the end of the 1990s, rank Austria about in the middle of the OECD with respect to the strictness of employment protection legislation (EPL). Recent policy initiatives have aimed at increasing the flexibility of non-standard types of employment contracts. Restrictions on temporary employment in tourism and agriculture have been eased, and private job placement agencies are now allowed to act as temporary work agencies. The new severance pay scheme (see above) should also support more flexible labour allocation.⁵⁶ The portability of severance entitlements is likely to have a positive influence on labour mobility. Similarly the steady accumulation of entitlements – rather than discrete jumps after a sequence of longer employment intervals –

avoids incentives for dismissals or quits around pronounced hikes of entitlement. Some tightening of EPL has occurred, though, for blue collar workers.⁵⁷

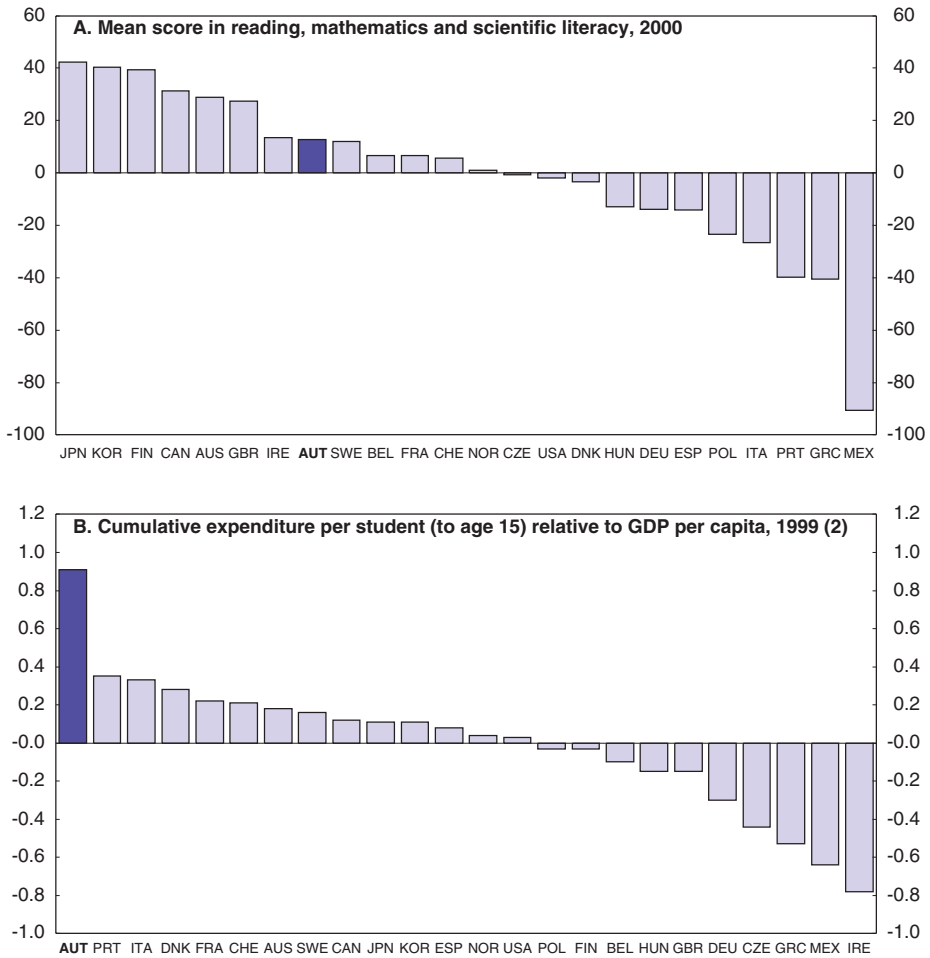
EPL, however, is more stringent, for employees aged 50 and over than for younger workers, as age is one of the social considerations that employers need to take into account in their dismissal decisions. Even if continued employment of an older employee appears to be at variance with business conditions, the management and the work council need to evaluate whether a younger employee could be dismissed instead. This provision may be a significant factor behind the low employment rate of older employees and the high utilisation of effective early retirement programmes within or outside the old age pension system. To the extent that easy channels into early retirement are available the dismissal provision is less binding. This is not true if early retirement is being curbed. Indeed, there is a secular increase in the share of employment disputes ending up in court cases. At the labour court of Vienna – where most cases are negotiated – settlement of about 70 per cent of total disputes were postponed to the next year in 2002, compared to about 40 per cent in 1987. Employment disputes (*Arbeitsverfassungsrecht*) almost doubled from 2001 to 2002, which might be related to the abolition of old-age early retirement on account of incapacity to work in 2001.

Recent legislation determines that the special dismissal protection of older people starts only after a waiting period of two years of continuous employment after recruitment, instead of six months as up to now. It needs to be seen whether this amendment will help to improve labour utilisation in the older-age bracket. In particular, the extension might be too modest to raise incentives for both employers and employees to engage in training that would lift the workers' productivity. Hence, it might be required further to revise dismissal protection for older people so as to increase the firms' incentives to employ older people. This might also be warranted in light of the tendency towards easier employment conditions for non-typical forms of employment such as fixed term contracts or temporary work. While this is likely to lower the costs of employment adjustments, care should be taken that the burden of adjustment is not concentrated on the group of low qualified "marginal" workers. At the same time the power of "insiders", working on permanent contracts, might increase if they feel more sheltered from unemployment than before.

Strengthening education

In the OECD's PISA study Austria figured above the OECD average with respect to the educational performance of 15 year old students. However, the fact that Austria stands at the top with respect to annual expenditure on primary and secondary schooling indicates that there is considerable scope for efficiency improvements (Figure 16).

Figure 16. **Educational performance of 15 year olds and spending on education**
Deviation from average¹



1. Average of countries in panels. A positive figure indicates above average.
 2. Expenditure on institutions per student from the beginning of education to age 15. Public and private institutions except for GRC, HUN, ITA, PRT, CHE which are public only and USA which is public and independent private only. See PISA source for details.
 Source: OECD, *Literary Skills for the World of Tomorrow – Further results from PISA 2000; Education at a Glance 2003*.

The PISA study suggests that certain institutional factors are of particular relevance for increasing the performance of schooling while limiting the impact of the students' socio-economic background on attainment. Many of the countries

that performed well in international comparison have been shifting education policy and practice from a focus on inputs – the resources, structures and content of schooling – towards a focus on learning outcomes. With this approach schools are given the authority for organising their own programmes and are held responsible for them. Also, in several well performing countries the extent of educational differentiation between schools is limited. There is scope to improve the performance of the Austrian school system on all of these scores. Differentiation of students by school types based on specific levels of performance takes place at younger age and is more pronounced than in some well performing countries. The degree of school autonomy in organising the learning environment differs across Austria, and there is a significant positive correlation between the level of school autonomy and student performance. Also, Austria shows one of the highest variations in school performance within the OECD. First initiatives have been taken to increase the degree of school autonomy, notably in budgeting. While progress has been made to develop quality standards for educational attainment in some areas, mandatory country-wide educational targets against which the performance of schools can be assessed on a regular basis have not been established. Against this background, a commission (*Zukunftskommission*) was set up for the purpose of making suggestions on how to shift the system further from input orientation toward focusing on learning outcomes.

With economies being based increasingly on education and knowledge, life-long learning is gaining importance.⁵⁸ In the Austrian context, the potentially beneficial role of life-long learning is reinforced by the prospect of a rapidly ageing society and the desire to increase employment opportunities for both women and persons aged 50 and over. As is apparent from the recent introduction of the general tax allowance for training, improving the skills of the workforce ranks high on the government's agenda, and various programmes are offered by the Ministries of Education and of Economics and Labour for this purpose. However, a number of conditions need be met to secure that resources are spent in an economically efficient way. Knowledge of the effectiveness of the different programmes of adult learning has been up to now rather partial, as evaluation of training and education is sparse.⁵⁹ Hence, programme evaluation needs to become a regular tool on which the policy makers' decisions can be based determining in which areas resources should be expanded or reduced. Using vouchers more widely would help in this respect by strengthening the scope for a market mechanism. Moreover, efforts should be made to arrive at a better integration of different training and education programmes. For example, in some instances active labour market programmes on the one hand and upgrade or supplementary education programmes on the other hand provide the same type of training, although the two are handled independently. Labour market programmes are developed and funded in the Ministry of Economics and Labour, and education programmes are funded by the Ministry of Education and the states. Bundling

resources and more co-ordinated programme design, based on programme evaluation, is likely to raise the effectiveness of adult training and to generate savings in the general government budget. In particular, more links should be established that provide an option for the unemployed to develop further the skills obtained in labour market programmes by participating in upgrade education programmes.

More generally, the *Zukunftskommission* on education reform should serve as a policy advisory board on how to increase the effectiveness and the range of life-long learning opportunities. The council could be used to improve the connections across various educational paths, and foster co-ordination between the bodies that are responsible for designing and funding adult learning and training. Recent policy initiatives also include the widening of income tax allowances for employees engaging in adult learning. This measure is likely to improve incentives for both employees and employers to invest in training. However, as the expected returns to training depend importantly on the lengths of future employment, it is also necessary to take action of the type addressed in this chapter to lengthen the average period of employment within the overall life cycle.

Box 4. Labour and product market reform – an overview of progress

This summary reviews progress in labour and product market reform since the Jobs Strategy recommendations were made for Austria in 1997. For competition related recommendations see Box 9 in Chapter IV.

Earlier proposals	Action taken since 1997	OECD assessment/ recommendations
I. Increase wage and labour cost flexibility		
<ul style="list-style-type: none"> Encourage wage differentiation, greater plant-level bargaining and opening clauses. Facilitate the employment of older workers and reduce incentives for early retirement. 	<p>Greater flexibility agreed in some sectors. Changed wage profile for white-collar workers.</p> <p>Subsidies introduced for employment of older workers and fines for dismissals. Relaxation of conditions for part-time pensions.</p> <p>Reduction of social charges for older workers.</p> <p>Severance pay made more employment friendly with monthly payments into retirement accounts.</p>	<p>Encourage the next step toward genuine opening clauses within the collective bargaining framework.</p> <p>Encourage wage negotiations which seek to take account of the special situation of older workers. Make unemployment benefits for older workers more closely follow market wages.</p> <p>Monitor the situation.</p>
II. Increase working-time flexibility and ease employment security provisions		
<ul style="list-style-type: none"> Reform regulations underpinning inflexible working practices. Liberalise terms for renewing fixed-term contracts Facilitate part-time and casual work. 	<p>Law governing hours of work liberalised allowing more flexible organisation of working time for industries taking advantage of this (e.g. metal). Greater flexibility agreed in some collective contracts.</p> <p>Restrictions reviewed and assessed to require no action.</p> <p>Extension of obligation for employers to pay social security contributions extended to self-employment and to casual jobs. Subsidised training leave targeted more tightly. Restrictions for part-time employment in the public sector eased.</p>	<p>Review effects of regulations and, when necessary, open possibilities for flexible agreements.</p> <p>Keep situation under review.</p> <p>Review the introduction of social security contributions for casual jobs and self-employment with a view to supporting the transition from unemployment to employment. Liberalise restrictions on working time by occupation. Reconsider subsidies for part-time employment of older people.</p>

Box 4. Labour and product market reform – an overview of progress
(cont.)

Earlier proposals	Action taken since 1997	OECD assessment/ recommendations
	Strict dismissal protection (<i>Kündigungsanfechtung</i>) for older people valid only after a waiting period of two years.	Consider abolishing <i>Altersteilzeit</i> .
<ul style="list-style-type: none"> Reform dismissal protection. 	Existing regulations reviewed and assessed to require no action.	Keep situation under review.
	Strict dismissal protection (<i>Kündigungsanfechtung</i>) for older people valid only after a waiting period of two years.	Relax regulations for older employees.

III. Reduce disincentives for labour market participation; foster job mediation

<ul style="list-style-type: none"> Reduce the incentives for early retirement. 	<p>Early retirement restricted. Incentives for early retirement pensions reduced.</p>	<p>Consider further means to curb early retirement in the short term and strengthen longer-term measures (stricter eligibility criteria, higher actuarial discounts for pension benefits). Abolish institutional segmentation of pension system. Reduce replacement rates of the pay-as-you-go system. Replace severance pay by company-based funded pensions.</p>
	<p>Unemployment benefits for older people will be temporarily increased by 25 per cent (<i>Arbeitslosenübergangsgeld</i>).</p>	<p>Measure should be phased out soon.</p>
	<p>Unlimited extension of unemployment benefits for participants in ALMPs provided by the PES.</p>	<p>Apply strict criteria for extending unemployment benefits for participants in ALMPs</p>
<ul style="list-style-type: none"> Reduce unemployment benefits to seasonal workers in the tourist industry. 	<p>Eligibility conditions tightened.</p>	<p>Monitor and proceed with reforms.</p>

Box 4. Labour and product market reform – an overview of progress
(cont.)

Earlier proposals	Action taken since 1997	OECD assessment/ recommendations
<ul style="list-style-type: none"> Reduce disincentives to take up work in social assistance programmes and develop in-work benefits. 	<p>Unemployment benefits and assistance are now gradually decreased for temporary employment, rather than immediately withdrawn. For unemployment insurance: waiting period introduced, the required minimum employment period lengthened, maximum duration of benefits increased.</p>	<p>To lower marginal effective tax rates at lower income levels, further examine possibilities to raise earnings disregards while simultaneously lowering benefits rapidly as people approach full-time employment. Develop in-work benefits in the context of greater wage differentiation. Widen job acceptance criteria with respect to skills. Abolish extended durations of unemployment benefits for older people.</p>
<ul style="list-style-type: none"> Give greater emphasis to active measures and less to passive measures. 	<p>Subsidies now paid to employers for employing those on unemployment assistance. For those on leave, a subsidy is paid if an unemployed is hired to fill the job or if training is taken up.</p> <p>Financial aid to firms and the unemployed for training and integrating the unemployed is being expanded. Target groups narrowed for promoted employment in social and health occupations. Subsidies for employment no longer associated with regional infrastructure investment.</p> <p>Temporary work agencies are allowed to conduct job placement and private placement regulations were eased.</p> <p>Subsidies for apprenticeship training introduced.</p>	<p>Monitor to see whether the restriction to take on unemployed is administratively feasible and that leave is not abused and becomes costly for the economy.</p> <p>Focus the measures narrowly on problem group. Evaluate effectiveness of schemes.</p>
		<p>Monitor.</p>
		<p>Monitor.</p>

Box 4. Labour and product market reform – an overview of progress
(cont.)

Earlier proposals	Action taken since 1997	OECD assessment/ recommendations
	Child benefits extended with respect to duration, eligibility and size.	Restructure in favour of child care facilities. Better integrate the various employment services, including the provision of social assistance. Introduce contestability of PES-services.

IV. Improve labour force skills

- | | | |
|--|--|---|
| <ul style="list-style-type: none"> • Preserve and restore the attractiveness of the dual vocational training system, clarify its relationship to higher education. | <p>Curricula for some apprenticeships revised and new occupations introduced. Health insurance contributions for apprentices waived and work hours of apprentices liberalised. Procurement contracts to be linked to training. Tax break granted and injury insurance contribution waived for companies taking on apprentices. Financial assistance to institutions organising additional vocational training.</p> | <p>Continue to revise vocational training curricula and occupations. Avoid attaching subsidies and procurement to training. In support programmes for youths who have not found apprenticeships, ensure that market forces are important in determining the type of training to be offered.</p> |
| <ul style="list-style-type: none"> • Shorten and reform higher education and focus it on more occupational-oriented studies. Extend role of new higher level schools (universities for applied sciences, <i>Fachhochschulen</i>). | <p>New university legislation allows for shorter study periods. Tuition fees introduced for students. More output-oriented budgeting being phased in.</p> | <p>Examine potential for moving some study fields to the new institutes of higher education. Shorten higher education and make it more occupationally oriented. Continue with reform of universities. Link funding to performance.</p> |

Box 4. Labour and product market reform – an overview of progress
(cont.)

Earlier proposals	Action taken since 1997	OECD assessment/ recommendations
V. Enhance creation and diffusion of technological know-how		
<ul style="list-style-type: none"> Foster venture capital markets and reduce regulatory barriers. 	<p>Stock exchange merged with options and futures markets. Vienna exchange now to link with Frankfurt. New single regulator for financial markets. Voluntary take-over code introduced. Programmes to encourage venture capital and business angels.</p>	<p>Lower effective taxation of equity. Widen the potential for investment funds to take equity in enterprises. Focus public financial support programmes on complementing private funding.</p>
<ul style="list-style-type: none"> Stimulate the diffusion of technology 	<p>Technology package being implemented which seeks to raise level of R&D. Clusters to be promoted in basic research and employment of scientists in industry subsidised. Competence centres being established.</p>	<p>Continue with basic reforms of the university and tertiary sector to encourage greater integration with the economy and increased productivity of research funding.</p>
VI. Support an entrepreneurial climate		
<ul style="list-style-type: none"> Facilitate the establishment of new enterprises 	<p>Regulations governing commencement of a trade liberalised (<i>Gewerbeordnung</i>). Relaxed restrictions on opening large-surface shopping centres to protect local shops. Costs of establishing SMEs lowered.</p> <p>Abolishment of stock exchange turnover tax. Establishment of unified financial market supervisor.</p>	<p>Continue to examine regulatory impediments and improve procedures especially at <i>Länder</i> level. Further liberalisation of trades law and of hours of trade.</p> <p>Monitor effectiveness of new institutional structure.</p>
<ul style="list-style-type: none"> Reform bankruptcy law to facilitate reorganisation. 	<p>Reform to bankruptcy law, changing governance incentives and powers of individual creditors including a lowering of potential personal costs associated with bankruptcy. Re-organisation procedures established with financial sanctions for directors if bankruptcy follows.</p>	<p>Monitor effects of reorganisation law. Consider extending protection to companies under restructuring. Improve discharge procedures allowing faster re-entry to business life of an entrepreneur.</p>
<ul style="list-style-type: none"> Planning approval needs to be simplified. 	<p>Approval procedures simplified and in some states down to three months.</p>	<p>Monitor the effectiveness of the new procedures and continue reform. Complete the one-stop-shop permission process.</p>

Notes

1. Austria joined the EU in 1995.
2. Austria's export share to Germany increased from 37 per cent in 1988 to 39 per cent in 1993.
3. The countries under consideration are Denmark, Belgium, the Netherlands, Sweden and Ireland, the same as those considered in Figure 3 above.
4. See OECD (1998a, 2001a).
5. A decomposition of the evolution of labour force participation rates by the Secretariat shows that between 1990 and 2000 the change in the age distribution reduced the Austrian participation rate by some 0.8 per cent.
6. Between 1990 and 2002 the registered unemployment rate for persons aged 55 and older increased from 7.1 per cent to 11.2 per cent for males and from 6.0 per cent to 11.5 per cent for females. Over the same period the total unemployment rate rose from 5.4 per cent to 6.9 per cent (definition excluding self employed).
7. According to the statistics of the Austrian Social Security Association the entry age into old age retirement stood at 62.2 and 59.4 years for males and females, respectively.
8. The average effective age of retirement is based on labour force survey data and derived from the observed decline in participation rates over a 5-year period for successive cohorts of workers aged 40 and over.
9. In the employment statistics, people who do not work in the second phase of an *Altersteilzeit* spell are counted as employed.
10. See Nickell, S. and S. Nunziata (2000).
11. See OECD (2001a).
12. OECD (2003b).
13. Gross spending on research and development in Austria has increased continuously from the beginning of the 1980s. The Austrian government is targeting to increase gross R&D spending to 2.5 per cent of GDP by 2006, and endorses the EU target of 3 per cent by 2010. On the issues involved, see Sheehan, Jerry and Andrew Wyckhoff (2003), Pilat *et al.* (2002) and Aiginger, Karl (2003).
14. With respect to tertiary education see OECD (2001a).
15. Spending on *Altersteilzeit* totals 28 per cent in terms of outlays for "activating" labour market measures in a broad sense, with activating "passive" unemployment benefits added to spending on active labour market measures.
16. See Breuss, Fritz (2001).
17. See OECD (1999).

18. The number of federal civil servants was reduced from 166 491 (end of 1999) to 155 173 (end of 2002). The number of federal school and university staff increased from 59 809 (end of 1999) to 59 889 (end of 2002). For schools and universities compensatory saving measures such as lower payments for special tasks of teachers were introduced. The number of tenured civil servants of spun-off organisations, excluding Post and Telekom Austria, increased from 3 226 (end of 1999) to 3 901 (end of 2002).
19. See OECD (2002a).
20. Subject to the targeted fiscal balance, additional spending is admissible if it is covered by additional revenues.
21. Legal procurement procedures are set out in the Federal Procurement Act and are subject to control by the Federal Procurement Office (FPO). Tender provisions regulate the procurement of works contracts, supply contracts and service contracts by public authorities and certain related entities from the private enterprise sector, notably in network industries. During tendering procedures involving a federal authority every tenderer can call upon the FPO to protect his interests. The FPO may issue a decree either to stop the tendering procedure or to cancel decisions of the tenderee. In order to ensure the transparency of tendering procedures, tenderers also have to discharge extensive duties of notification towards the European and national procurement authorities.
22. See Schneider, Martin (2002).
23. See Doubek, Claudia (2002).
24. See Doubek, Claudia (2002) *op. cit.*
25. Changes in the allocation of responsibility for social assistance payments can be achieved via a contract between the federal government and the states in accordance with paragraph 15a of the federal constitutional law.
26. Older people living in nursing homes can be charged with up to 80 per cent of their pension by the nursing institution. The remainder is financed out of social assistance benefits.
27. For an account of the arrangement governing employment and remuneration of teachers, see Rossmann, Bruno and Pia Netuschill (2002). The paper takes stock of the state of administrative reform in Austria between 2000 and 2002.
28. See Aufgabenreformkommission (2001).
29. The findings of the Convent are planned to feed into the negotiations for the next tax sharing arrangements between the federal government, the states and the communities. The next tax sharing agreement will come into effect from 2005 onwards.
30. See McLure, C.E. (2000) and Oates, W.E. (1999).
31. These figures, based on CEEP (2000), conform well to earlier estimates contained in the OECD's International Regulation Database (see Nicoletti *et al.*, 1999). Information in this database also suggests that the size of the public enterprise sector in Austria is large, both in size and scope, by OECD standards.
32. Gonenc *et al.*, 2001; OECD, 2002c.
33. For Austria, Gugler (1998) provides evidence that internal rates of return amongst public enterprises are well below rates in private firms even when the effects of various background factors have been controlled for.
34. The steel industry was, and remains, characterised by high mark-ups by international comparison and cost-plus regulation often discouraged innovation efforts. Moreover it

- had become the norm that managers were appointed not only for their formal qualifications but also with an eye to their political orientation (Aiginger, 1998).
35. Some caution is warranted here, though. In addition to governments' determination to divest, the size of such proceeds is influenced also by overall share prices at the time of privatisation. The 5½ per cent of GDP is the total of proceeds in each year since 1990 relative to GDP in the corresponding year (see OECD, 2002). According to Aiginger (1998) divestments of central government assets worth some 2 per cent of GDP were made during the second half of the 1980s, but in some of the largest transactions the ownership was transformed to other public-sector entities (the Austrian National Bank in the case of the central mint and local governments and public companies in the case of the *Verbund* energy company).
 36. Both scenarios differ in assumed employment rates. The baseline scenario, which yields a more favourable spending path, assumes that the employment rate increases from 67 per cent in 2000 to 76 per cent in 2035, while the less favourable scenario assumes that the employment rate increases to only 72 per cent. See *Kommission zur langfristigen Pensionssicherung* (2002).
 37. This measure re-installs the situation prevailing until 1997, when the rate was lifted to its present level.
 38. See OECD (2003c).
 39. European countries that qualify for investment consist of the EU and the EFTA. Eligible stock market capitalisations must not exceed 30 per cent of GDP. This advantages holdings of Austrian stocks whose capitalisation is low by international comparison.
 40. For an account of company based pension funds see Url (2003).
 41. Administrative costs are limited to a maximum of 3.5 per cent of contributions plus a maximum of 1 per cent of administered funds. Additional expenses have to be stated in the contract.
 42. At present, part-time employment can be distributed over an admissible time span of up to 6½ years such that the employees work full-time in the first years and cease working in the remainder of this period. Working time reductions up to 60 per cent of the previous level qualify for financial support. At least 50 per cent of the income loss due to working time reductions is compensated by the government. The scheme can be utilised by males and females from 55 and 50 years onwards, respectively. If part-time employment is taken in blocks of full-time and no work, participants in the scheme are statistically accounted as employed during the no-work phase.
 43. Econometric evidence for Austria indicates a significantly negative effect of the duration of extended eligibility periods for receiving unemployment benefits on the transition out of unemployment for the long-term unemployed, both male and female. Moreover, longer benefit duration might also lead to higher unemployment entry. See Winter-Ebmer. (2003). The relevance of this relationship is also evident from various studies for other OECD countries. For references see OECD (2003d).
 44. See OECD Directorate for Employment, Labour and Social Affairs, Review of family-friendly policies in Austria, Ireland, and Japan, DELSA/ELSA(2003)5/ANN2. For a comprehensive analysis of the Austrian child care system see the main text of this document.
 45. Re-entry rates into the labour force appear to be positively related with the level of earnings prior to the non-participation spell. See Lutz (2003).

46. For example, for a couple with primary and secondary earnings equalling 100 per cent and 33 per cent of the earnings of an average production worker (APE) and two children aged one and four years, full-time child care costs amount to 25 per cent of the APE.
47. For school children, out of school hours care includes the care provided by all day schools.
48. See OECD (2003e).
49. Between 1997 and 2000 investment in child care facilities was increased.
50. The long run elasticity of real wages to unemployment has been found to be significantly higher in Austria than in other countries, notably Germany, France and Italy. See Roeger and in't Veld (1997).
51. For blue-collar workers per capita wages in Austria decline in the age group 60 and older. However, employment rates for this group almost collapse. Hence, the earnings profile might be subject to a selection bias in that only people working either fewer hours or on less well paid jobs stay in employment.
52. See OECD (1998b). In most other OECD countries wage profiles (based on 1995 figures) are less steep and hump shaped with earnings peaking at around age 50. Controlling for educational attainments of cohorts the tendency of age-earnings profiles to slope downward late in working life weakens but is not reverted.
53. The inter-sectoral wage dispersion appears to be relatively stable, see Mesch (2002), and Hofer *et al.* (2001). At the same time, high labour cost differentials across sectors appear to be weakly related to relative labour demand patterns. In particular, inter-sectoral cost differences have been found to be largely unrelated to labour qualification, see Pollan (2001). Similarly, empirical evidence suggests that for most sectors in manufacturing negative employment growth coincides with substantial growth in earnings. See Mesch (2002) *op cit.* The author finds a coincidence of positive income growth with an increase in employment for only two manufacturing sectors out of 11 over the period from 1980 to 1994. Wage flexibility was found to be low by international comparison. See Hofer and Weber (2002).
54. Empirical evidence for the metal industry suggests that Austrian enterprises have less scope than German and Italian firms in differentiating pay and setting incentives. See Auer *et al.* (1997).
55. See Auer and Welte (2001). There have also been conflicting views between employers and unions about the distributional consequences of allocations to employees for the purpose of supporting vocational training.
56. The transition to the new severance pay system affects labour costs differently across sectors, as previously exempted branches, like those with high seasonal fluctuation of workers, are now liable for severance pay. This will require some adjustment in relative wages across sectors.
57. There is a general tendency to put blue collar workers more on a par with salaried employees, and this has led to some tightening of EPL for blue collar workers. For example, in the iron and metal industry the notice period for dismissals was lengthened to equal that of salaried employees. Notice periods for blue collar workers are laid down in collective agreements between the social partners and hence differ between industry sectors. By contrast, notice periods for salaried employees are harmonised and coded in the labour law. Since 1999 a working group of the social partners negotiates on a harmonisation of regulations.

58. See OECD (2001c). Major features of ongoing university reform have been considered in the 2001 *Economic Survey on Austria*.
59. For evaluation studies of active labour market programmes, see OECD (2001a) and Weber and Hofer (2003).
60. In-depth analyses of product market competition in Austria have been included in earlier *Surveys* (1990, 1994 and 2001). However, because political and analytical attention to competition issues and regulatory reform has increased considerably only over the past decade, the availability of cross-country evidence was scarcer when these studies were undertaken.
61. Parallel imports of products that are protected by intellectual property rights consist of genuine products (as opposed to counterfeits) which are sold without the consent of the rights owner in a country.
62. This study also argues that Austria stands to gain considerably from the imminent enlargement of the EU. Simulations presented in Breuss (2001) show that the size of these gains can be expected to be larger than in any of the other current EU member states. See Box 1 above.
63. Trend MFP growth has edged down by $\frac{1}{4}$ percentage point in the course of the 1990s.
64. In addition, various more narrowly focused laws exist, such as the Local Supply Act (*Nahversorgungsgesetz*) and those regulating competition in network industries. The Federal Procurement Act (*Bundesvergabe-gesetz*) aims at ensuring competition in public tenders.
65. The CCom consists of eight professional members, half of whom are appointed upon a proposal by the social partners.
66. Mergers must be notified to the Cartel Court if the combined relevant turnover of the involved undertakings is above € 300 million worldwide and above € 15 million in Austria, and if the total turnover of each of at least two participating undertakings is above € 2 million.
67. Certain agreements have been exempted by a Regulation issued by the Ministry of Justice, including agreements concerning joint purchasing and joint R&D.
68. Agreements may be considered de minimis. This is the case if parties have a combined market share of five per cent on the national level or even up to 25 per cent in a local sub-market.
69. The Cartel Act is not explicit about the criteria to be employed in the assessment of this, but states that the justifiable interests of both the binding and bound enterprises as well as those of consumers must be taken into consideration.
70. As part of the preparation of its 1997 Green Paper on vertical restraints the European Commission conducted a survey of member states' policy in this area, which provided information also on the practical application of the rules (European Commission, 1996). For Austria, this study revealed that in 1994 some 800 agreements were notified and that not a single one of these resulted in any action. In fact, the Cartel Court had not decided any cases concerning vertical restraints at that time.
71. Approximation of Austrian law concerning restrictive agreements to EU rules also would be advisable to fully realize the benefits of decentralised enforcement of EU law under Regulation 1/2003.
72. Still, insofar as the relevant conduct affects intra-Community trade, the exemptions under the Cartel Act are limited by the potential application of EU law.

73. Some have argued that transparency suffers from a preference on the part of the FCA to settle cases on the quiet without the involvement of the Cartel Court (Böheim, 2003).
74. The recent *EconGas* joint venture is a case in point. This case, which was the first to be reviewed under the new merger control regulation, involved the incumbent federal energy company, OMV, and five of the regional utilities. The new company, *EconGas*, has a market share well above the 30 per cent threshold that is considered to constitute a dominant position. Nonetheless, both the FCA and the PP withdrew their initial applications for examination on the basis of certain concessions from the involved companies. As a result, the case was settled without an examination by the Cartel Court and with no accompanying press release from the FCA that could motivate the clearance.
75. Criminal sanctions for collusive tendering were maintained, probably reflecting that such practice has been blatant and widespread in the past, notably in the construction sector.
76. It must be emphasised, though, that a leniency programme would need to be attuned to other elements of the enforcement regime. In particular, a lenient treatment is likely to be less potent if the perceived risk of disclosure is low in the first place, or if the sanctions that could be envisaged by infringers are disproportionately small compared with the gains from unlawful conducts.
77. No information is available on prices paid by large-scale consumers since these are typically set in bilateral contracts. However, price reductions have been particularly large in this segment according to the assessment of E-Control.
78. This might reflect, in part, price discrimination by incumbents in order to fend off entry and consumer switching in those segments of the market where the price elasticity is highest. In Austria, however, pre-liberalisation prices for business customers were much higher than for households, and the greater decline for the former group has only meant a convergence to the relative price levels seen elsewhere.
79. It seems uncertain whether the latter restriction is compatible with the non-discrimination rules under EU law.
80. For example, when co-signing the deal the responsible minister emphasised the importance of having found a “red-white-red” solution.
81. According to estimates provided by AC Nielsen, concentration is considerably higher, the two largest retail groups – REWE and SPAR – having a market share of two-thirds.
82. For example, increasingly efficient marketing and inventory management methods and larger trade areas facilitated by easier access to individual transportation are forces that work towards concentration and larger units.
83. Kelly and Gosman (2000) find evidence that in the United States high buyer concentration tends to reduce manufacturers’ profitability in competitive industries but not in sectors with weak upstream competition. Beyond the objective of short-term cost-minimisation, the rise in own brands could be another, more strategic, reason for retailers to squeeze suppliers’ profit margins if possible. If they succeed, such practices are likely to be detrimental to competition.
84. The “non-specialised stores” part of the distribution sector is the one where economies of scale and scope are likely to be most important, as it includes large-format outlets such as hypermarkets and department stores. This segment is considerably smaller in Austria than elsewhere and less than half the size in Finland, Ireland and

- Norway. The obverse to this is that the “specialised non-food stores” segment (excluding pharmacies) is relatively larger than in other countries. In this branch, as well as in specialised food stores, productivity is comparably high in Austria. As for food stores, this is due, in part, to a high penetration of (German owned) discount chains.
85. Environmental considerations could be addressed in general zoning regulations.
 86. The Shop Closing Act foresees that provincial governments may grant privileges to family-operated stores (maximum weekly opening time of 80 hours), shops in tourist resorts and shops in areas where more than half the population work outside the area. In addition, shops in railway stations, airports, theatres and petrol stations are exempted or operate under less restrictive regulations. In its general sales promotion the VIVA group of convenience stores, which are attached to some 160 of the OMV petrol stations, is offensively presenting itself as an around-the-clock supplier of a limited range of groceries – including fresh bread on Sunday mornings when the Shop Closing Act – with a few exemptions – prevents even bakeries to be open (www.omv.at). This is somewhat ironic given the fact that OMV is controlled by the government.
 87. For example, in a recent investigation the Danish Competition Authority (2000) concluded that RRP’s were more widespread than had been thought previously. In specialised non-food stores, RRP’s applied to more than half the lines. There was a significant positive correlation between the prevalence of RRP’s and high prices by international standards. The study estimated an unfavourable welfare effect of ½-1 per cent of GDP.
 88. The principle of regional exhaustion was stated in the European Court of Justice’s (ECJ) ruling in the so-called Silhouette case. This case involved the importation into Austria, and hence the Community, of sunglasses first sold by the Austrian company Silhouette in Bulgaria. The company brought an action against the parallel importer for breaching its trademark rights in Austria, and the ECJ upheld the contention.
 89. The previously required certificates of qualification were abolished altogether for wholesale and retail trade. Moreover, the scope for fulfilling qualification requirements *via* accredited practical experience was extended and steps were taken towards introducing a one-stop shop principle for setting-up new firms.
 90. There is some variation in the findings of different studies, though. One study (European Observatory for SMEs, 1997) reports an average entry rate between 1988 and 1996 of almost 9 per cent in Austria, only slightly lower than the simple average for all EU countries and higher than in for example Finland and Belgium. In contrast, the European Commission (2000b) finds the start-up rate in Austria to be well below average, and lower than in Finland and Belgium. Both of these studies rely on national data, where cross-country comparability may be relatively weak. Scarpetta *et al.* (2002) provide comparable data on enterprise demography for 10 OECD countries over the period 1989-94. While Austria is not included, the smallest entry rates found in this study are larger than those from the Austrian Chamber of Commerce reported above in Figure 8. Comparable data for nine EU countries (not including Austria) were published in early 2003 by Eurostat (Hult, 2003). Enterprise birth rates (1998-2000) were in the range of 7 to 11 per cent across the nine countries.
 91. A recent Eurostat study of business demography in nine EU countries indicates that the typical two-year survival rate is around 75 per cent (Hult, 2003).
 92. Such geographical restrictions also apply to driving schools. Before 1 October 2002 learners were bound to pass the driving test in their local police jurisdiction, which meant that they were also geographically restricted in their choice of driving schools.

While this has now been changed, regulations prevail that limit driving instructors' right to supply their services outside narrowly delimited local areas. Also, recently introduced rules significantly raised the number of lessons required to pass a test for becoming a driving instructor, thereby increasing entry costs. Regulations such as these clearly impair competition and lead to higher prices. According to studies by the Chamber of Labour, driving-school fees are some 20 per cent higher in Austria than in Germany.

93. Given the dependence on hydro-electricity, emissions depend on rainfall. This factor was responsible for a significant part of the fall in emissions from the electricity sector between 1990 and 1999.
94. IEA (2003).
95. WIFO (2001), quoted in BMLFUW (2002).
96. Capros *et al.*, (1999).
97. IEA (2002) and Criqui *et al.*, (2002).
98. There would be additional transitory costs related to the required structural change.
99. As shown in the 2001 *Survey*, this policy would be very expensive.
100. IEA (2000).
101. Taxes paid by households reached € 174 per ton of oil equivalent (toe) for fuel oil, € 118 per toe for natural gas and € 428 per toe for electricity in 2000 (IEA, 2002).
102. OECD (2001a).
103. Capros *et al.*, (1999).
104. Indeed, if taxation of fuels were equalised on the basis of carbon content, then the taxation of gasoline and diesel could be reduced by 80 per cent with no increase in emissions, on the basis of sectoral cost curves.
105. European Commission (2001).
106. OECD (2002e).
107. Several landfills were affected, notably the *Fischer* and *Berger* sites. The latter was completely renovated at a cost of EUR 20 per ton.
108. A cost-benefit study has been commissioned to review the decision to ban the landfill of untreated waste by 2004 (*Umweltbundesamt*, 2001). The study compares the total costs, including externalities, of all available methods to dispose of waste. For landfills, the study adds to the externalities a risk factor, which is equal to the cost of cleaning the site if it were to prove to be contaminated. Under this scenario, landfill is costlier than all other methods of disposal.
109. IEA (2001).
110. RDC (2001).
111. Eurostat (2002).
112. OECD (2002), and OECD International Trade by Commodity Statistics electronic data base.
113. Welfare gains flowing from the reduction in tariff barriers by the European Union as a whole are estimated to exceed 1 per cent of GDP in countries such as Malawi and Tanzania (UNCTAD and *Commonwealth Secretariat*, 2001).
114. Gallezot (2002).

115. In the presence of a large degree of distortion in developing country agricultural markets, the small terms-of-trade loss could be transformed into a welfare gain, even if the domestic distortions are not ended.
116. Anderson *et al.*, (2001); Roberts *et al.*, (2002).
117. OECD, (2003).
118. EC (1999). This result is conditional on the particular assumptions used in the simulations, notably that it is the imperfectly competitive sectors that exhibit increasing returns to scale.
119. Fischler (2001), Agricultural Policy for the Future Changing Concerns, Changing Objectives. Speech to the 29th North American/European Union Agricultural Conference, Salzburg, 19 October 2001.
120. European Commission (2002).
121. The key element of the new, reformed CAP is introducing a single farm payment for EU farmers, independent from production, although limited coupled elements may be maintained to avoid abandonment of production. Further details about the reform can be found at http://europa.eu.int/comm/agriculture/mtr/index_en.htm.

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BASIC STATISTICS OF AUSTRIA, 2002

LAND

Area (1 000 km ²)	84	Major cities (1 000 inhabitants):	
Agriculture (%)	31	Vienna	1 550
Forest (%)	43	Graz	
		Linz	226
		Salzburg	143
		Innsbruck	113

PEOPLE

Population (1 000)	8 033	Labour force ¹ (1 000)	4 302
Inhabitants per km ²	96	Employment ¹ (1 000)	4 067
Natural increase in population, 2000 (1 000)	1	Agriculture (%)	13
Net immigration, 2000 (1 000)	17	Industry (%)	24
		Services (%)	63

PRODUCTION

GDP, current prices (billion euros)	218	Origin of value added (%)	
GDP per capita (1 000 USD in current prices)	26	Agriculture	2
Gross fixed investment per capita (1 000 euros)	6	Industry	30
		Services	67

GOVERNMENT

Public consumption (% of GDP)	19	Composition of Federal Parliament:	Seats
General government total revenue (% of GDP)	51	Socialist Party	65
Public debt (% of GDP)	67	Austrian People's Party	52
		Freedom Union	52
		Greens	14

Last general election: December 1999

FOREIGN TRADE

Exports of goods and services (% of GDP)	53	Imports of goods and services (% of GDP)	51
Main exports (% of total merchandise exports):		Main imports (% of total merchandise imports):	
Machinery and transport equipment	43	Machinery and transport equipment	39
Manufactured goods	35	Manufactured goods	32
Chemicals and related products	10	Chemicals and related products	11

CURRENCY

Irrevocable conversion rate (1 euro)	13.7603	Euros per USD:	
		Year 2002	1.06
		September 2003	0.89

1. Domestic concept.

Note: An international comparison of certain basic statistics is given in an Annex table.

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The economic situation and policies of Austria were reviewed by the Committee on 8 September 2003. The draft report was then revised in the light of the discussions and given final approval as the agreed report by the whole Committee on 3 October 2003.

•

The Secretariat's draft report was prepared for the Committee by Eckhard Wurzel, Friedrich Fritzer, Steen Daugaard, Richard Herd and Boris Cournede under the supervision of Andreas Wörgötter.

•

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