

BIS | Department for Business
Innovation & Skills

**EMPLOYMENT REGULATION,
EMPLOYMENT AND GROWTH :
CONSIDERATION OF
INTERNATIONAL EVIDENCE**

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EMPLOYMENT REGULATION, EMPLOYMENT AND GROWTH CONSIDERATION OF INTERNATIONAL EVIDENCE:

A: INTRODUCTION

1. In response to the House of Commons Parliamentary Question 98926 from Mr Chris Ruane MP for the Vale of Clwyd (below) Norman Lamb laid a short summary note on our assessment of the effect of regulation on employment and growth together with some of the more important pieces of evidence¹:-

‘To ask the Secretary of State for Business, Innovation and Skills, what statistical data his Department holds on the effect of employment regulation on economic growth; and if he will place a copy of such data in the Library’

2. This note picks out some of the key elements of that material, places it in a historical context and adds further information drawn from the blog of Professor John Van Reenan on this subject ‘It is time to move away from policy witchcraft and into an area where evidence is taken seriously.’ This we hope might be useful as background to the Enterprise and Regulatory Reform Bill.

B: HISTORICAL BACKGROUND

3. The OECD in its reassessment of its Jobs Strategy in 2006² concluded ‘there is no single combination of policies and institutions to achieve good labour market performance [...] this allows scope to tailor policy packages to suit national preferences with respect to equity risk-taking and other objectives.’
4. The economic and labour market structure or framework tends to be built upon the culture and tradition of the country with the development of the social protection system an important determinant. The UK approach to social protection has largely been based on the tax and benefit system and the ‘Beveridgean’ welfare state. It has never tended to rely upon employment regulation as a major element of its social protection system.
5. Therefore, there has been little general government intervention into the terms and conditions of employment. What legislation there was tended to be aimed at protecting vulnerable groups. For example, there were hours limits on groups who were (then) considered vulnerable – women and young people – and also sectoral minimum wages in industries where the bargaining power of the workers was considered weak. Also, it was only December 1965 that statutory redundancy payments were introduced.

6. This approach tended to be accepted by both sides of industry and it is only relatively recently that the trade unions have become greater advocates of regulation. Previously in some areas they considered that government intervention might supplant some of their labour market role.
7. Where there was general legislation it tended to be to promote equal opportunities. And indeed 'fairness' or horizontal equity is one of the features of the UK system. This is not only in employment regulation but also in the welfare state. For example, the UK has flat rate benefits. This tends to reflect a society where universal basic minimum standards provided by the state feature heavily. Compared to other countries the UK does not tend to favour certain types or patterns of work as 'standard' or 'typical'.
8. Consequently, compared to other countries the UK's employment regulation system tends to be both light and even – in line with the principles of optimal tax policy. Therefore, in the UK more than in other countries 'a job is a job' and forms of work that in other countries might be considered second class, atypical or non-standard are more generally accepted – by both businesses and workers.
9. Over time this light and even approach has tended to spread. Women are no longer treated in employment regulation as a 'special' case needing help. For older workers legislation such as the Default Retirement Age has been abolished. This is not to say that there are no groups – on the business or the worker side - that society favours through legislation. However, equal treatment tends to be the default and there seems to need to be a very good reason why a specific group should be favoured.
10. Against the historical background the government in its programme for government 'Freedom, Fairness, Responsibility'³ committed to

'review employment and workplace laws, for employers and employees, to ensure they maximise flexibility for both parties while protecting fairness and providing the competitive environment required for enterprise to thrive.'

and it also identified a specific group that it wanted to favour.

'The Government believes that strong and stable families of all kinds are the bedrock of a strong and stable society. That is why we need to make our society more family friendly.'

11. The Employment Law Review was set up to deliver these coalition commitments. This review is to last the lifetime of the parliament. It is focusing on three stages in the employment relationship⁴:-
 - **taking people on**, to make it as easy as possible to recruit your first, and subsequent, members of staff

- **managing your staff**, removing inflexible processes and requirements and allowing grown-up conversations between employers and their staff, and;
- **ending employment**, allowing that to happen in a way that is flexible and economically efficient, whilst remaining fair for individuals.

C: HOW THE EVIDENCE DEVELOPED

12. A key element of the Employment Law Review is the collection and collation of the evidence. This involves not only a consideration of the overall system but also how the various elements of the system fit together.
13. This latter element is important because as the OECD concluded it is important to tailor the policy package so that the system as a whole functions successfully. Two implications follow. First, it is not possible to import wholesale policies from other countries as they might disrupt the efficiency of the system. Secondly, as well as academic and theoretical evidence it is also necessary to see how the policies function and interact in real life. Therefore, evidence from practitioners and also practical experts in the field is very important.
14. One strand of evidence used to inform developments in employment regulation in the UK has been international best practice on labour market policies – including the labour market effects of employment regulation. International comparisons are particularly important as a way of assessing the effects of employment regulation because legislative changes tend to be glacial in their speed. And with little change in the system it is difficult to isolate the specific effects associated with employment regulation.
15. The OECD has been the main source of international comparisons of labour market policies and there has been close collaboration with the OECD over the past generation. One example of this is the OECD Index of Employment Protection. It was derived by the OECD from analytical work in the UK in the late 1980s/early 1990s undertaken in order to understand and gauge the effects of proposals from the European Commission in respect of first the Social Charter and then the Social Chapter that eventually was included in the Maastricht Treaty.
16. However, the view of international best practice itself has tended to evolve. Annex 1 sets out the OECD recommendations in relation to employment regulation over this period including both the original OECD Jobs Study published in 1994 and its reassessment which was published in 2006.
17. From these OECD statements it is clear that in 1990 not only was there a vigorous debate about what was the effect of ‘flexibility’ and ‘deregulation’ but also that there tended to be differences within the OECD. Annex 2 sets out some OECD comments about the UK at the time that brings this out.
18. **‘Progress in Structural Reform’** - which was a supplement to the 1990 Economic Outlook - commented favourably on the ‘determination and vigour’ with which the UK had pursued supply-side reforms in this area. Whereas, **‘Labour Market Policies for the 1990s’** which was published by the Manpower and Social Affairs Committee (MSAC) was more

measured commenting that ‘some observers regarded the focus [on flexibility] as biased by employers’ interests’.

19. From this point the MSAC Committee – which had previously tended to promote and favour progress through policies that focused on internal flexibility and ‘insiders’ - began to give greater weight to external flexibility and ‘outsiders’. Its conclusion in this document was ‘Well-designed labour market policies often have the advantage of achieving efficiency and equity objectives simultaneously’ [and] ‘In the future a reasonable balance will have to be found between internal and external flexibility.’
20. However, it noted that there were ‘forceful counter-arguments to deregulation’ and these differences were one of the reason Ministers mandated in May 1992 the labour market and economic committees in the OECD to carry out the Jobs Study in order to help the 35 million people unemployed in OECD countries. The study was completed in 1994 and endorsed by OECD ministers.
21. The main conclusion of the **OECD Jobs Study** was:-

‘No avenue of research was excluded in seeking both the causes of unemployment and appropriate solutions. Numerous gaps in available data made this task more difficult and a number of questions persist. But several converging indications point strongly to an insufficient ability to adapt to change as the fundamental cause of employment difficulties in OECD countries.’
22. For employment regulation policies this was not an endorsement of deregulation but rather stressed the importance of better regulation. It balanced efficiency with equity considerations and involved a shift towards a greater focus on external flexibility and on integrating ‘outsiders’ through the use of incentives and economic methods.
23. The conclusion of the **Reassessment of the OECD Jobs Strategy**⁵ was that ‘Many of the policy recommendations are unchanged from the original Jobs Strategy: they have stood the test of time and relevance. But the reassessment has also yielded new insights and policy lessons’. [It also suggested that] ‘The successes achieved by some OECD countries show what can be done if there is sufficient political will to reform.’
24. The most relevant insights and policy lessons for employment regulation and working time arrangements are:-
 - It is vital to remove existing barriers to labour force participation among women, older workers and under-represented groups more broadly. As regards women, several family friendly policies have shown their worth. They include flexible working patterns, appropriate tax incentives, adequate but not overly long paid parental leave, good quality, affordable child care and more sharing of caring responsibilities between men and women. Concerning older workers, remaining

disincentives to continued work embedded in old-age pension systems and various pathways into early retirement need to be removed.

- It is time to grasp the nettle of employment security versus flexibility. Too often, countries have opted to ease the conditions governing temporary jobs while leaving those governing permanent jobs unchanged. While this may deliver some short-term job gains, it leads to growing duality in labour markets and hinders investment in training, and thereby productivity growth. Fortunately, there are better alternatives to hand. One such is so-called 'flexicurity' [...]
- Policies to expand labour demand are crucial. This involves pricing back into employment the lower-skilled who are excluded by tax, social contributions or institutional arrangements [...]
- Finally, experience shows that there is **no single golden road to better labour market performance**. There is more than one model of success to hand from which to take inspiration to fit specific national circumstances and history. However, this does not imply that anything goes. The successful performers share some common features, not least an emphasis on macroeconomic stability, adequate incentives for all labour market participants and strong product market competition.

25. Following the OECD Job Study Reassessment in 2006 the **OECD Employment Outlooks of 2007-2011** also provides some insights and policy lessons for employment regulation. These have the advantage of throwing some light on the recent economic crisis. However, in some cases the results are not as well established. Employment Outlook in:-

- **2007:** 'the clearest result [...] is that too strict statutory protection for regular contracts appears to dampen **productivity growth**, most likely by restricting the movement of labour into emerging high-productivity activities, firms or industries'. [Much more uncertain results are that] 'parental leave appears to increase average productivity, in part by allowing workers with family responsibilities to maintain their links to the workforce in general, and to their existing jobs in particular' [and] 'a well-designed activation policy for jobseekers can potentially replicate some of the positive productivity impacts associated with generous unemployment benefits, such as improving the quality of job matches, while also promoting employment.'
- **2008:** 'Combating **informal employment** requires a comprehensive approach that reduces the costs and increases the benefits to businesses and workers of operating formally and ensures that regulations are adequately enforced.' 'Strict employment protection legislation increases incentives for informal employment in countries with limited enforcement capacity.' 'Labour inspectorates should be adequately resources and trained.' 'Sanctions should be large enough to act as a deterrent.' [and] 'Coordination between tax/social security, labour inspection and other agencies is vital.'

- **2009:** ‘Even in a recession there is considerable **hiring.**’ ‘Stricter employment protection for regular and temporary workers tends to reduce workers flows in and out of unemployment. For permanent workers, the negative impact of employment protection on unemployment outflows (i.e. hires) dominates the negative impact on inflows (i.e. separations), resulting in an increase in the level of structural unemployment.’ [that is likely to result from the recession].
- **2010a:** [There is a] ‘large cross-country variation in gross worker reallocation’ [flows]. [And] ‘greater labour reallocation is associated with a lower incidence of **long term unemployment.**’ ‘Large gross job and worker flows partially reflect better job opportunities available to workers due to an enhanced job-matching process’. [and] ‘Stringent employment protection for regular contracts is estimated to have a large and statistically significant effect on worker reallocation’. ‘In a jobs crisis the fraction of workers losing their jobs in total separations tends to increase significantly [...] Under these circumstances , it is important to put in place an adequate policy mix to sustain income during job search and support the transition towards new jobs.’
- **2010b: Part time work has further increased over the past decade and is predominantly voluntary.** Part time employment is a growing share of total employment ‘with substantially higher shares in [...] the UK.’ ‘In a majority of cases more than half of part timers are prime aged women.’ ‘Since the early 1990s most OECD countries have introduced new laws [...] requiring part time workers to receive comparable wages and working conditions on a pro rata basis.’ The UK’s tradition of equal treatment and equal opportunities meant that it did not have to alter its legislative structure much, if at all, to comply.
- ‘Overall, part time work promotes higher labour force participation and can be a viable alternative to inactivity for many, if appropriate incentives are in place.’
- ‘Women who voluntarily work part time appear to be satisfied to trade off wages, future earnings potential and job security for more family friendly working time arrangements. However, for some it does not and in recent years – including in the UK – involuntary part time work has risen. ‘The bargain between [part time] penalties and [family friendliness] may be motivated by short-term time constraints and may fail to take into account the longer term adverse impacts of part time work on poverty risk, career progression and retirement income.’
- ‘Rights for full time workers to request part time work are also widespread in OECD countries’ – including the UK where there is a broader right to request flexible working arrangements. The OECD tentative conclusion is that ‘statutory rights to part-time work may be achieving at least one of their aims, helping workers with caring responsibilities to reduce their working hours. However, the few studies

that examine the impact of the laws suggest that their impact may be modest, at best’.

D: LESSONS FROM THE OECD JOBS STUDY AND REASSESSMENT

Overall performance

26. In general over the past 25 years the UK has been judged by the OECD as a major reformer across the whole range of labour market policies and particularly employment regulation and welfare to work policies.
27. These reforms have tended to be based around ‘What Works’ and appear to have been successful. The Jobs Study Reassessment judged the UK to be one of the ‘successful’ employment performers and that ‘While it had its critics, the record shows that those countries [which include the UK] which implemented its [the original Jobs Study] recommendations outperformed those who did not.’

Strictness of Employment Protection

28. The OECD Employment Protection index combines information on the specific statutory provisions in three areas; regulation on temporary forms of employment; specific requirements for collective redundancies and protection of regular workers against individual dismissal.
29. The result of the UK’s ‘light and even’ approach to employment regulation is that, within the OECD, only the US and Canada have less strict employment protection regulations. The UK’s regulatory system is also much less onerous than in Brazil, Russia, India, China and South Africa (the BRICS countries) and the other developing countries that have been measured by the OECD. There has been some increase in the strictness of employment regulations since the early 1990s but it has been relatively small and it has led to the UK swapping places with Canada.

Working Time Arrangements

30. The UK’s ‘light and even’ approach also means that there are very few legal restrictions on working time arrangements relative to other countries. Therefore, the range of types and patterns of work in the UK that can be offered by employers and sought by workers is substantial. [This is set out in Wells⁶ for the early 1990s and the essential features remain.]

Perception versus Reality of Employment Regulation

31. The OECD employment protection index is based on legal requirements. However, perceptions can differ substantially from the reality. This is true

both of the perceptions of businesses about the legal requirements they face and the perceptions of workers about the range of types and patterns of work that are available.

32. There are a number of reasons for this. Many are associated with a lack of information. There is no clear, easily accessible exposition of what businesses can do (rather than what they can't do) for example. But it may also be because the system as a whole lacks coherence, and is complex. Finally, most of the comparisons in this area are relative. It may be that although employment regulations are less onerous than in other countries they are quite restrictive in absolute terms.
33. There is evidence that perceptions do differ from reality. There is (old) evidence that businesses in manufacturing and retailing in the UK are less likely than in some other EU countries to regard hiring and firing laws as an obstacle to employing more people.
34. And the OECD⁷ concluded that 'Relaxation of statutory employment protection in case of individual and/or collective dismissals [...] may partly explain the drop in the share of firms in [the UK (1993)] who perceive restrictions as a constraint on hiring practices.' However, even after this drop – from 44% of manufacturing businesses in 1989 – 25% still considered hiring/firing practices to be very important or important in holding back employment.
35. The latest World Bank report on doing business – which is based on perceptions - tends to confirm that UK businesses tend to regard employment regulation as fairly unrestrictive [in 2009 the overall index number for the UK was 10 in an index that covered 0-100]. However, both the index and the country ranking did not provide as positive a picture as the OECD index that is based on the reality of the legislation.
36. There are also differences between the perception and reality for workers. Again it seems that the perceptions may be worse than the reality. Job insecurity was considered in the 1997 OECD Employment Outlook and it concluded that 'A widespread and, in some countries, very sharp increase in the number of individuals perceiving employment insecurity took place between the 1980s and the 1990s. However, [...] jobs seem as stable in the 1990s as they were in the 1980s.'
37. In addition, perceptions of insecurity were high in Japan, the US and the UK despite these countries (then) having low unemployment. It is also noteworthy that in the UK and some other countries it is those with the highest level of education who are more likely to report their job as insecure. Obviously other factors are also at work.

Effect of Employment Regulation on the Structure of the Labour Market

38. The most recent (2009) OECD work on employment regulation concluded that 'overly strict regulations can reduce job flows, have a negative impact on employment of some groups of workers (notably youth), encourage labour market duality and hinder productivity and economic growth.'
39. This is despite the evidence [OECD 2006] suggesting that 'Employment Protection Legislation (EPL) appears to fulfil its stated purpose, namely protecting existing jobs. However, EPL also restrains job creation [...] A number of studies find that strict EPL tends to compromise the employment prospects for those groups that are most subject to entry problems, such as young workers, women and the long term unemployed, by reducing labour turnover and hiring.'
40. The UK's light and even system does not display these signs of an overly strict regime. The lack of restrictions on hiring and firing is compatible with the high level of turnover that characterises the UK labour market – around 1 in 5 of the workplace move into a job each year and a similar proportion leave a job. Also, even in recessions, most of these flows into and out of work are voluntary.
41. In addition, just as there are incentives to avoid or evade high taxes so there are incentives to avoid overly strict regulation. There is relatively little sign of this in the UK. The proportion of temporary work – which tends to be less attractive to workers - is low and largely voluntary and there is little sign of use of this form of work as a way of avoiding the regulations on permanent work.
42. Similarly, as the size of the black economy tends to be small in the UK relative to other countries there is little sign that UK businesses are trying to evade strict regulation by employing people outside the formal sector. Of course there is some avoidance and evasion and we need to minimise it. However, it is small.
43. As well as having a very dynamic labour market compared to other countries the UK also has one of the most diverse. The lack of regulation on work patterns provides greater opportunity for businesses and workers to decide on types and patterns of work that suit them.
44. And they seem to take up these opportunities. There is evidence that the UK has the widest range of types and patterns of work⁸ – whether it is where they work or when they work in the day, the week or the year.
45. For example, despite the fact that the average UK worker works around 5% less than the OECD average number of hours per year [1,649 compared top 1,749 hours in 2010], the diversity of hours worked means that the average is relatively meaningless because so few people work

exactly an average number of hours. Also, both full time and part time encompass such a range of different patterns of work that those terms are also relatively meaningless as a summary description.

46. This dynamism and diversity is one of the factors contributing to the fact that the UK has one of the highest employment rates in the world. Also, rates for every main age and sex category are higher than the OECD average. The greater choice of work patterns in the UK and the ease of getting a job increase the possibility that jobs are available to a wider range of people with a wider range of characteristics and responsibilities.
47. Consequently, the dynamism and diversity of the UK labour market – which is partly a function of the employment regulation regime – contributes substantially to the family friendly nature of the UK labour market. More people can combine paid work with the rest of their life.
48. It also provides greater opportunities for a wider range of people – including disadvantaged groups – to take up a job. So, for example, it might be possible for someone who relies on hard work and ambition more than skills and qualifications to find a job that suits those characteristics.

Labour market policy interactions.

49. The Jobs Study Reassessment recommends as one successful model ‘flexicurity’ – an approach that facilitates hiring and firing decisions while also providing efficient re-employment services such as intensified job search assistance. Denmark is the country that is generally considered to epitomise ‘flexicurity’ but it could equally apply to the UK. The UK’s system includes an employment regulation system that promotes dynamism and diversity of work patterns and combines it with an aggressive and comprehensive activation – the promotion of jobsearch - approach to people on both unemployment and other non-employment benefits.
50. Where the UK system tends to differ from Denmark is that there is a greater focus on job search in the UK system and less focus on more intensive Active Labour Market Policy interventions such as training. This greater focus on job search seems to be compatible with the ‘light and even’ employment regulation system in the UK and the fact that the UK labour market is more decentralised and individualistic than the Danish system. So, job-matching rather than up-skilling may be more important. As the (then) analytical director of the UK Department of Social Security in an OECD/EU conference in 2000⁹.

‘I do not dissent from the paper’s emphasis on the need for good education systems and I endorse the cautious advocacy of training linked to employment. But of even greater importance is the need to keep people in touch with the labour market. This is reflected in the attitudes of people out of work and claiming benefits. The most frequently cited reason for not looking for work is a belief, often erroneous, that there are no jobs available. Particularly where there are large concentrations of people

dependent on out of work benefits, the information network about the state of the labour market will be poor. More active benefit policies for these people should provide better information about the state of the labour market, measures which can be more effective in reducing joblessness than more expensive interventions.

51. Where the approach of the UK and Danish system do coincide is in focusing on quantity – employment – adjustments. Other countries have systems that focus more on price – wage – and productivity adjustments. The social partnership model in Germany, for example, focuses more on the ‘internal’ than the ‘external’ labour market and their collective co-ordinated approach tends to deliver amongst other things more wage moderation. This is an example of a system where a more restrictive employment regulation system can be successful because all the actors in the labour market – workers, employers and government – work together to deliver economic success.
52. However, it does tend to mean that the employment regulation regime is too restrictive for certain parts of the labour market. Therefore, Germany has tended to provide a less restrictive tax and regulatory regime for the small firm and low paid sector. However, even though less restrictive than the rest of the German labour market this sector is still more restrictive than the institutional settings in the UK.
53. Evidence¹⁰ suggests that the UK is right to focus on quantity rather than price adjustments and is unlikely to be able to import the wage moderation that has characterised Germany.

Government’s role in promoting flexible working time arrangements.

54. The UK’s ‘light and even’ regulatory approach removes barriers to businesses and workers negotiating hires, working time management and separations. However, it also results in complex and diverse working patterns – even with the same firm. This suggests that there may be a more active role for government – at least in providing a framework or code of practice – that enables the decentralised individual negotiations to be carried out efficiently.
55. The proposals on the right to request flexible working and settlement agreements can be seen as examples of this. However, as mentioned above, the design of such proposals needs care otherwise there may be unintended consequences.

E: LESSONS FROM THE RECESSION AND BEYOND?

56. There is growing evidence that the UK labour market has shown greater resilience than other countries during and after the recession and that the combination of a ‘light and even’ employment regulation system and a successful activation regime has contributed to this.

57. UK presentations by Wells¹¹ suggest that the trough of employment in this cycle was equivalent to 4 million higher than the trough of the 1980s recession. In addition, given the size of the output fall in this recession the fall in employment is much less than most commentators were expecting.
58. A key element of this success has been the continued focus on increasing the labour supply of people previously on lone parent and disability benefits by getting them to look for work and promoting and providing job search help so that they can find a job. This has led – despite the recession – to the numbers on ‘inactive’ benefits falling to a 20 year low. In addition, the historic trend towards lower employment in retirement and early retirement has been reversed. And all of this has occurred during a major recession.
59. In addition, the labour market policy response to the recession was in line with the UK’s tradition. Funding for Jobcentre Plus was increased so that they could maintain the intensity of the jobsearch regime. This could be considered the labour market policy equivalent of automatic stabilisers. Rather than subsidise the maintenance of jobs the approach was to try to ensure that people who had lost their jobs were re-integrated into work as soon as possible. Also, there was extra help for the existing unemployed and workless, particularly young people and the long term unemployed.
60. This focus on maintaining the efficiency of job-matching contrasts with the German approach where the focus was more on the maintenance of jobs in the internal labour market. Their work sharing policies were in line with the social partnership approach where all three of the labour market actors – government, business and labour – accepted the need to bear some of the cost of the recession through government income supplements, wage moderation and lower profits.
61. Also, in Germany the Hartz reforms of their public employment service also seems to have been more effective than in the past at re-integrating people who were already or became jobless.
62. The OECD ascribe some of the UK’s relative success to ‘the progressive improvement of activation policies for recipients of unemployment and other income-replacement benefits that was achieved by a number of countries during the past two decades helped to dampen the increase in unemployment during the crisis. The Netherlands, Germany and the United Kingdom are examples of such countries.’¹²
63. In addition to the improvement in activation it is also likely that the ‘light and even’ employment regulation regime in the UK contributed. Recruitment actually rose during the recession and has remained high. This is likely to signify that the natural turnover that is part of the UK labour market – and which is partly dependent on the employment regulation regime – has provided opportunities for people on benefits to take up.

64. Nominal wage growth relative to both the past and other countries has been slower since 2007. However, estimates¹³ show that for a stereotypical worker – single with no children, full time in the private sector – take home pay was still second only to Switzerland in the OECD.

F: POSSIBLE IMPLICATIONS FROM THE EVIDENCE FOR THE EMPLOYMENT LAW REVIEW.

65. The evidence suggests that the UK employment regulation system at the start of the Employment Law Review was in good shape. However, both the new evidence that is emerging from the OECD Jobs Study Reassessment and beyond and also the priorities of the government suggested that there were possibilities for improvement.
66. The evidence and the priorities of the government suggested that reforms to the level of the employment regulation system and its composition would be beneficial.
67. On the level of regulation there are 3 areas that are being considered:-
- Whether the balance of the employment protection system had shifted too far in favour of existing workers. A recent change was the extension of the qualifying period for unfair dismissal from one to 2 years.
 - How to improve the family friendliness of the system and, in doing so, increase the efficiency of the labour market and the participation of mothers through flexible parental leave and the extension of the right to request flexible working.
 - In a very decentralised and individualistic labour market is there a role for government to set a framework which will enable businesses and workers to negotiate freely to their mutual benefit? Amongst the possibilities in this area are the extension of the right to request flexible working and also settlement agreements.
68. On the composition of the employment regulation system the Reassessment of the OECD Jobs Study suggested three ways forward:-
- A more coherent and integrated set of labour market policies that considered the interaction between regulation and activation.
 - Consideration of the coherence and interactions within the employment regulation system itself from end to end. For example, from the start of a dispute to its resolution.
 - Consideration of the efficiency of the compliance and enforcement regimes and the efficiency of the institutional settings.
69. However, in order to increase the efficiency of the employment regulation and enforcement systems per se it is necessary to have a detailed consideration of what works. In addition, given that the employment regulation system is so dependent of the culture and tradition of each

country it is not possible to import wholesale policies from another country. They will need to be adapted.

70. Therefore, although this consideration of international best practice can identify broad directions of travel, delivering an efficient and effective system requires much more in depth consideration. It is for this reason that not only were the usual consultations undertaken but also a range of other information was gathered including formal and informal consultations.¹⁴

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ANNEX 1: OECD RECOMMENDATIONS ON EMPLOYMENT PROTECTION LEGISLATION AND WORKING TIME ARRANGEMENTS

Progress in Structural Reform: OECD 1990

There has been widespread recognition that the path to lower unemployment rates lies neither in reducing labour supply, nor in public-sector job creation nor in subsidising private industry with a view to protecting employment. Hence, in practically all OECD countries labour-market policies have gradually been re-orientated towards improving efficiency of these markets. Government have tried, in varying degrees and each in its own way, to increase: i) the extent to which the markets are subject to competitive pressures; ii) the qualifications of workers; iii) the incentives for workers to search for jobs; and iv) the incentives for business enterprises to hire workers. The corresponding measures, which have not been easy for governments to take, include:

- Paring down statutory restrictions on the freedom of businesses to reduce their workforce thereby reducing the risks of hiring;
- Facilitating short term employment contracts and part time work.

Measures to increase the efficiency of labour markets depend to a considerable degree on the particular ways in which labour-market institutions and practices have evolved. However, the broad directions of future reforms can be outlined in general terms:

- More flexibility in employment contracts and lower costs of dismissal protection in order to reduce disincentives for expanding the workforce.

Labour Market Policies for the 1990s: OECD 1990

Since its creation in 1961, the history of the Manpower and Social Affairs Committee has been closely linked to the spread of active labour market policies in OECD Member countries.

A critical assessment of labour market policies since 1961 would suggest a mixed record. This was reflected in changing public perceptions of these policies. They were hailed in the 1960s...In the 1980s they were rediscovered as an important micro-economic instrument to remove rigidities and barriers to structural change but this did not make them particularly popular because it implied a focus on efficiency at the expense of equity. The situation may be increasingly required it to change yet again in the 1990s. Labour market policies may be increasingly required to reintegrate the long term unemployed and other disadvantaged groups into a market... Providing opportunities for all to compete in the expanding but rapidly changing economies of the future would revive and strengthen the idea that labour market policies can achieve efficiency and equity objectives simultaneously.

Increasingly, the general view gained ground that if any lasting progress in the return to full employment were to be achieved – other than by prolonged policies of demand restraint forcing wage- and price-setters to modify their behaviour – some fundamental changes in institutions, attitudes, and rules and regulations governing the socio-economic system in general, and the labour market in particular, were required. High and quasi-fixed labour costs, rigid wage setting procedures, generous social protection and rules and practices which shielded some workers in secure jobs at the expense of others in unstable jobs, were some of the factors that were perceived as reducing the capacity of national economies to adjust to new international market signals to profit from new economic opportunities. This led in the late 1970s and 1980s to a long series of OECD policy statements urging micro-economic reforms and ranging from positive adjustment policies, to the need for structural adaptation, to flexibility in product and factor markets and to structural surveillance....

The emphasis in labour market policies on flexibility and adjustment objectives did not meet with general approval. In fact, some observers regarded the focus as biased by employers' interests. However, the deregulation movement also comprised areas like competition policy, price fixing, procurement practices, where deregulations were clearly fundamental. What was at stake was something more fundamental. It can best be described by the distinction suggested by Dobell (1981). He observes that in the evolution of the welfare state, there was a shift of emphasis from the mere redistribution of income through tax/transfer systems towards direct interventions in the structure of the system that generates income and wealth. The latter aims at altering the distribution of primary incomes (for instance through minimum wage floors) or the terms on which individuals or enterprises participate in the economic system (for instance, through quantity restrictions on imported goods). This approach, therefore, is designed to alter market mechanisms and to resist (or modify) market signals. The deregulation movement was triggered off by this latter approach of superimposing social goals directly on economic activities. It was not meant to dismantle all regulations, many of which, in fact, are indispensable to make a market economy work.

In modern labour markets there are normally two sources of flexibility: functional (internal) flexibility allows workers who enjoy job security and company-based training to accept technological change, to be redeployed and to adjust to new work assignments; numerical (external) flexibility permits enterprises to adjust the size of their total workforce to fluctuations in product demand...In the future...a reasonable balance will have to be found between internal and external flexibility. The challenge for public policy will be to preserve the advantages of internal labour markets, but at the same time to prevent access to these markets from being limited to certain workers and completely foreclosed to others – hence to ensure that a certain degree of external flexibility is maintained.

The OECD Jobs Study: Paris 1994

Recommendation 3: Increase flexibility of working-time (both short-term and lifetime) voluntarily sought by workers and employers.

Less rigid arrangements for daily, weekly, annual and life-time working hours could meet both enterprise requirements and worker aspirations. They would permit firms better to exploit their productive capacities by matching production more closely to shifts in demand. Workers and their families would also gain from new working –time arrangements tailored to their individual preferences or family circumstances. The type of working-time flexibility sought by firms may not always coincide with the aspirations of workers. The best way to resolve such conflicts is through negotiated solutions at de-centralised levels. In some countries legislative changes to taxation and social security provisions are also needed.

One important attraction of greater work-time flexibility is its potential to integrate working-time reduction with new patters of life-long learning. More flexible working-time arrangements would also facilitate greater lifetime participation of women.

Recommendation 6: Reform employment security provisions that inhibit the expansion of employment in the private sector.

Employment protection legislation is designed to discourage dismissals by raising the cost to employers of releasing workers. But it can also make employers more reluctant to hire new workers. Countries, mainly in Europe, which have particularly stringent legislation generally have a high rate of long-term unemployment, and employers frequently resort to temporary contracts and other ‘non-standard’ forms of employment to meet their needs for greater work-force flexibility.

At the same time legislated employment security, along with job guarantees negotiated by collective bargaining also bring benefits. Employment security through long-term contracts can encourage investment in on-the-job training.

A balance has to be struck between allowing employers greater freedom in decisions to hire and fire, and ensuring that sufficient employment security for workers and firms to be willing to invest in long-term training and protection for workers against unfair dismissal.

Boosting Jobs and Incomes – Policy Lessons from Reassessing the OECD Jobs Strategy

Recommendation B6: Facilitate family-friendly arrangements.

Family-friendly policies including childcare support, as well as working-time arrangements which help reconcile work and family life, should be implemented so as to remove barriers to employment for those with family commitments.

Pillar B: Removing barriers to employment of under-represented groups and reducing segmentation of labour markets.

Employment of under-represented groups can be stimulated by eliminating incentives to retire early and changes in workplace practices...

Older workers face a range of barriers to employment... Employment opportunities for older workers have also been held back by ageism in the workplace, mandatory retirement practices, widespread use of seniority pay and lack of training opportunities.

...tax reforms and family friendly policies can increase female employment...

Women also face obstacles through tax disadvantaged, poor design of family-support policies and lack of part-time jobs... Lack of suitable parental leave provisions, which help to reconcile work and family responsibilities, also reduces female participation, Moreover, childcare costs may act as a barrier for women to seek work outside the home.

...and policies to avoid school failure plus closer links between education and work can reduce youth unemployment.

Failure of the school system to provide **all** young people with basic skills needed to operate effectively in the labour market makes school-to-work transitions difficult. And effective approach has been sustained intervention to avoid early school failure, sometimes starting before the compulsory school age. Also, countries where education alternated with work experience – with wages set at the appropriate level – tend to have low youth unemployment. And, outside the education system, the provision of targeted employment programmes and remedial education and training may help young jobseekers find a job.

Finally, in some countries, promoting transitions to formal employment is of paramount importance.

...The incidence of informal employment depends heavily in certain countries on i) taxation of low-paid (formal) employment vis-a-vis taxation of income from activities with a high incidence of undeclared work, like small businesses; ii) the stringency of employment regulations (which may make employers reluctant to formalise employment relationships) iii) the extent to

which formal employment entails a right to pension and unemployment benefits (to make formal employment attractive to workers themselves); and iv) enforcement of the rules of the game.

Recommendation C6: Facilitate the adoption of flexible working-time arrangements.

Obstacles in labour legislation which impede the emergence, through employer-employees agreements, of flexible working-time arrangements should be removed; tax and social security provisions should not discriminate against part-time work or other flexible arrangements which help reconcile work and family life and promote gradual work-to-retirement transitions.

Recommendations C7 & C8: Make sure that employment protection legislation helps labour-market dynamism and provides security to workers.

C7: Employment protection legislation should be reformed in countries where it is overly strict, by sanctioning unfair dismissal (for example by prohibiting dismissal on the basis of discrimination with respect to gender, age and ethnicity), but reducing constraints on dismissals for economic reasons; severance costs and administrative procedures should be made more predictable so as to reduce judicial uncertainty; reasonable dismissal notice periods should be provided so as to help laid-off workers find new jobs.

C8: Regulations on fixed-term and temporary contracts may need to be relaxed in some countries; in order not to aggravate labour market duality and thus undermine labour market performance in the long terms, a more balanced treatment between temporary and permanent contracts could be pursued, with one option being that dismissal protection rights grow in line with seniority

Recommendation C9: Promote transitions to formal employment.

Transitions to formal employment should be promoted through: lower taxes on low-paid employment going hand-in-hand with better compliance of other taxes (notably on small businesses); reforms of labour regulations and business registration requirements, to make firms more prone to create formal jobs; and closer ties between social protection entitlements and work to encourage workers to declare their job.

Pillar C: Adapting employment regulations and wage-setting practices and promoting product-market competition can support job creation and boost real wages.

While tax and welfare reforms facilitate labour market participation, it is equally important that policy allows labour demand to expand so as to accommodate higher supply.

Labour demand can be stimulated through flexible working-time arrangements agreed between the employer and employees...

Consistent with the Jobs Strategy recommendations, many OECD countries have taken measures to promote flexible working-time arrangements and part-time work. The stated purpose of the measures has often been to enable greater flexibility for employers to better match working-time schedules with production requirements. Ensuring greater choice for workers regarding work schedules has also helped promote labour force participation of certain groups, notably women with young children. However, more work is required to better understand the determinants of hours worked, why they differ across countries and the effects of greater flexibility on job quality.

...and employment protection regulation consistent with the need for labour market dynamism.

The link between the stance of employment protection and aggregate unemployment is uncertain in theory, and in practice is highly dependent on the specific national context. However, there is evidence that too-strict legislation will hamper labour mobility, reduce the dynamic efficiency of the economy and restrain job creation. This may worsen job prospects of certain groups, like young people, women and the long-term unemployed. Reforms in this area have proved difficult, as workers resist measures that are perceived to reduce their job security. Hence, reforms have often been partial and even sometimes counter-productive. Indeed, partial reforms – which facilitate recruitment on temporary jobs while leaving permanent contracts untouched – have been more common and may have boosted job growth in the short run. But they have also contributed to create temporary-job traps in some countries and risk perpetuating dual labour markets, with adverse effects on labour market performance in the longer run.

Innovative reform avenues have been found so as to instil greater labour market dynamism while also providing workers with adequate protection. Making legal procedures more predictable has been one useful approach as this reduces the risk to employers of judicial uncertainty about the cost of firing. Another one is ‘flexicurity’, i.e. an approach that facilitates hiring and firing decisions while also providing efficient re-employment services, such as intensified job-search assistance, and income support to workers in the event of lay-off. Yet another requires employers to pay regular earnings related contributions into individual severance accounts that can be accessed by the worker whatever the type of contract, in the case of lay-off. This implies that, when the worker leaves the firm, the employer does not incur any special firing costs.

Exploiting policy interactions can improve employment performance...

Although the Jobs Strategy was formulated in terms of 10 separate broad policy guidelines, the experience over the past decade has highlighted the existence of interactions between different structural policy areas... The analytical evidence suggests that exploitation of these potential synergies can lead to improved employment performance.

ANNEX 2: OECD COMMENTS ON UK POLICIES AND PERFORMANCE

Progress in Structural Reform: OECD 1990

By the later 1970s the United Kingdom had one of the least responsive economies in the OECD area. Over the last decade, supply-side policies have been pursued with greater determination and vigour than in most other Member countries. Deregulation of product and factor markets has increased competitive pressures on management and workers.

Statutory regulations governing the functioning of the labour market have been relaxed, and restrictive work practices lessened... The 1988 Employment Act ...repeals most legislation that still discriminates in employment matters between men and women, removes working-time restrictions for young people, and eases rules governing dismissal of staff.

Labour Market Policies for the 1990s

Employment and Redundancy Legislation: In the United Kingdom the trend has clearly been to ease the circumstances in which employers can dismiss workers without risk of being called to account by the courts. Under the Employment Protection (Consolidated) Act 1978, workers were not able to appeal to Industrial Tribunals [now Employment Tribunals] on the grounds of unfair dismissal if they had been employed by their firm for less than 6 months. In 1988 this period was extended by order to in year's employment and in 1985 it was again extended to years; these periods were felt to be sufficient to enable an employer to judge whether newly hired workers met requirements. In an attempt to discourage frivolous complaints from being brought before the tribunals, the government has proposed that powers be given to enable the chairmen of tribunals to have 'pre-hearing reviews' and to order that either party to a dispute pay a deposit before a full hearing takes place. It has also been proposed that the period after which a discharged employee can demand a written statement of the reasons for dismissal be extended from the present 6 months to two years' employment.

Working-time arrangements: Recent trends in working time can be viewed as reflecting a number of apparently contradictory trends. On the one hand, government want to deregulate so that work can be carried out to meet market requirements. On the other, there is a continuing wish of workers and their representatives to reduce individual working time – but not, however, to reduce earnings in proportion – arguing that will create employment opportunities for the unemployed.

[Evidence from the UK is hardly mentioned in this section as the UK did not generally have any policies to reduce working time although there were hours reductions agreed through national collective bargains. Nor were there any general legislative policies on early retirement. However, there were some

small scale government programmes – Job Release Scheme and Job Splitting Schemes. Also for men aged 60-64 the unemployment benefit rules were relaxed in 1983 to become a de facto early retirement benefit. Part time working increased ‘partly spontaneously i.e. without any change in the legislative framework’ as the lack of regulation in this area in the UK enabled this form of work to grow. It was a similar story for temporary or fixed-term contracts where the lack of regulation meant there was the freedom to choose this form of work. However, as the rules on permanent work were ‘light and even’ firms and workers usually chose indefinite contracts.]

¹ The reference material comprised of:-

- A short summary note: Employment Regulation, Employment and Growth
- OECD: ‘Boosting Jobs and Incomes: Policy Lessons from Reassessing the OECD Jobs Strategy: 2006.
- Danielle Venn (2009): ‘Legislation, collective bargaining and enforcement: Updating the OECD employment protection indicators: OECD Social, Employment and Migration Working Paper No. 89: 2009
- Bill Wells (1992) “Does the Structure of Employment Legislation Affect the Structure of Employment and Unemployment?” UK EC Presidency Event on Labour Market Issues: Glasgow.

² OECD: ‘Boosting Jobs and Incomes: Policy Lessons from Reassessing the OECD Jobs Strategy: Paris 2006.

³ The Coalition: our programme for government. Freedom Fairness Responsibility.

⁴ *Flexible, effective, fair*: Promoting economic growth through a strong and efficient labour market. A BIS discussion paper September 2011.

⁵ Editorial of OECD Employment Outlook 2006: Boosting Jobs and Incomes.

⁶ See Bill Wells (1992) in Footnote 1 above.

⁷ Implementing the OECD Jobs Strategy: Member Countries’ Experience: OECD 1997

⁸ See, for example, Table 20 Page 78: Implementing the OECD Jobs Strategy.

⁹ A Comment by David Stanton pp 167-173 in ‘Policies Towards Full Employment’’: Proceedings of the Helsinki Conference January 2000: OECD

¹⁰ See, for example, Beatson ‘Labour Market Flexibility’ Department of Employment Research paper; OECD Employment Outlook 2004 and more recently OECD Employment Outlook 2011.

¹¹ 'Changes in the UK labour market: Cyclical versus Structural' & 'A History of the Claimant Count' both presented by Bill Wells of BIS at separate ONS/Labour Market Statistics User Group conferences in 2011 and 2012.

¹² OECD Employment Outlook 2011: page 21.

¹³ 'Taxing Wages 2011': OECD Paris 2012.

¹⁴ As well as academic and theoretical evidence it is also necessary to see how the policies work in the workplace. Therefore, there was an extensive canvassing of views from practitioners and also practical experts in the field. In addition, information was sought from a range of sources both formally and informally – through techniques such as crowd sourcing – and nationally and internationally.

And in order to maximise the chances of getting it right a wide range of people were consulted including regular consultation with a wide range of business stakeholders, trades unions, and legal and HR representative organisations but also including those who were not the 'usual suspects'.

Amongst the formal methods of consultation were:-

[The Red Tape Challenge in April 2011](#) which is set to run for two years until 2013. This Challenge aims to look at the stock of over 21,000 statutory rules and regulations that are active in the UK today. Everyone is invited to give their views whether as an individual, as a business, or as a representative body. The priority will be to focus on regulations that we know place the biggest burdens on businesses and society.]

Employment related law is a specific theme in the [Red Tape Challenge](#) and in October 2011, a particular focus was placed on looking for areas for simplification and removing burdens in employment law. During that spotlight period, we received almost 2,000 views on issues relating to 160 employment related regulations.

The link to the Red Tape Challenge on employment law is: - <http://www.redtapechallenge.cabinetoffice.gov.uk/employment-law/>

A report was also commissioned -

<http://www.bis.gov.uk/assets/biscore/employment-matters/docs/r/12-825-report-on-employment-law-beecroft.pdf> which was considered as part of the Employment Law Review and Red Tape Challenge.

In addition, because there was some interest in the concept of No Fault Dismissal there was a call for evidence and also some cases studies that tried to establish what was going on in some other countries.

<http://www.bis.gov.uk/assets/biscore/employment-matters/docs/d/12-626-dismissal-for-micro-businesses-call.pdf>

<http://www.bis.gov.uk/assets/biscore/employment-matters/docs/d/12-771-dismissal-for-micro-businesses-case-studies.pdf>

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