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# DECENTRALIZING WAGE SETTING IN TIMES OF CRISIS? THE REGULATION AND USE OF WAGE-RELATED DEROGATION CLAUSES IN SEVEN EUROPEAN COUNTRIES

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**Keywords:** derogation clauses; decentralized wage setting; times of crisis

## 1. INTRODUCTION<sup>1</sup>

Sectoral and intersectoral level collective agreements are a key feature of industrial relations in most Western European countries. Traditionally (inter)sectoral bargaining has had the function of homogenizing wages and working conditions for entire sectors or countries and taking them out of competition. Also, it brings stability to the relations between workers and employers and relieves company level actors from engaging in time consuming and possibly conflict-ridden bargaining processes. In recent decades, however, the rationale for such (inter)sector agreements has been questioned. In the context of the advancing globalization of competition there have been increasing calls for greater decentralization and flexibility in the setting of wages and working conditions, in order to allow firms to address their specific competitive needs and problems. This has, to a different extent in different cases, resulted in a process of ‘organized decentralization’ (Traxler 1995), referring to increased company-level bargaining within the framework of rules and standards set by (inter) sectoral agreements. Such decentralization has often concerned working time issues but it is also affecting wage bargaining, especially where non-basic wage elements are

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concerned (Keune 2006, 2008). In Germany, decentralization increasingly also seems disorganized as the binding power of sector agreements and their coverage rate are declining. The current economic crisis is sometimes argued to be a further argument to speed up decentralization of collective bargaining. Others, however, argue that the very instability of the crisis strengthens the importance of sectoral bargaining as it provides more stability.

A specific form of decentralization is the opening up of possibilities for companies, through various kinds of derogation clauses (opening clauses, hardship clauses, opt-out clauses, inability-to-pay clauses, etc.), to deviate from pay norms set under intersectoral or sectoral agreements, including minimum wages, when they suffer from temporary economic hardship. The reasoning behind such deviations is that they are an instrument that may permit companies to overcome temporary economic difficulties without resorting to (mass) layoffs. This may help to prevent workers from becoming unemployed, avoid costly lay-off procedures and preserve human capital for the company. These kinds of company-level deviations from (inter)sectoral wage agreements have received growing attention and interest in recent years in academic and policy debates in Europe, particularly since the present economic and financial crisis started to put many companies and jobs under pressure. However, it is also a controversial subject as such practices challenge some of the principles of collective labour law, the regulatory capacity of collective bargaining and the traditional structure and functioning of national collective bargaining systems in continental Europe. Furthermore, they may in principle lead to wage declines, to increased insecurity for workers and to an increase in low pay.

There is hardly any systematic information and analysis available concerning the various ways these deviations are legally regulated in different countries; the extent to which they are indeed included in intersectoral, sectoral and other agreements; what the conditions for their use are; and the extent to which they are actually used in practice at company level. The present article aims to fill some of this void. It provides a summary of the results of a comparative study on the regulations, practices and politics of wage derogation clauses in seven EU countries: Austria, Belgium, France, Germany, Ireland, Italy and Spain (see Keune 2010). In all seven countries multi-employer bargaining (*i.e.* sectoral or inter-sectoral bargaining) plays a major role, especially where wages are concerned. Inter-sectoral bargaining is of key importance in Belgium and Ireland<sup>2</sup>, whereas in the other five, as well as Belgium, sectoral bargaining is important.

The structure of this paper is as follows: in the next section a review of the laws that affect the possibility of using opening and other clauses concerning wages is provided. Section 3 discusses the use of such clauses in practice, while in section 4 the positions

<sup>2</sup> Ireland has a long history of national social pacts. However, the most recent central tripartite agreement collapsed in late 2009. The employers and trade unions subsequently adopted joint guidelines for the company level negotiations that would take its place, in this way maintaining some form of central steering.

of governments and social partners on these clauses are reviewed. Section 5 presents conclusions.

## 2. DEROGATION CLAUSES IN LABOUR LEGISLATION

The legal regulations concerning derogations differ substantially in the seven countries. In Austria, Germany and Belgium, the law does not explicitly foresee wage derogations. Rather it determines through a general principle of hierarchy that higher level agreements trump lower level agreements: the latter cannot contradict or go below the standards set in the former. However, the law in these countries does not explicitly exclude the possibility of derogation clauses either, making it possible, in principle, for employers and unions to incorporate such clauses in higher level collective agreements.

In France and Spain the law does deal specifically with wage derogations. In France, traditionally, the hierarchy of norms dictated that lower level agreements could not change for the worse from higher level agreements. This changed with the 2004 Fillon law, which determined that a lower-level agreement may deviate from the provisions of a higher level agreement unless such derogation is expressly forbidden in the higher level agreement. Four major issues are exempted from any derogation at company level: minimum wages, job classifications, supplementary social protection measures, and multi-company and cross-sector vocational training funds. Thus, as regards these four issues, company-level agreements may differ from agreements signed at branch level only in favour of the employees. However, the exceptions do not concern additional wage elements such as performance-related pay, shift work, night work, allowances for marriage or child-birth, or seniority payments. On these issues company agreements can deviate from higher level agreements unless these expressly forbid such deviations.

In Spain, since 1994, the Workers' Statute contains a mandate to include an opt-out clause in collective agreements at sectoral or inter-sectoral level allowing companies to adopt lower wages than those agreed at higher level when they temporarily undergo economic difficulties. Collective agreements adopted above undertaking level must contain the conditions and procedures for the application of such opt-out clauses, which are considered to be part of the minimum content of the collective agreement at that level. Most recently, the crisis-induced Royal Law Decree 10/2010 of 16 June, on urgent measures on the reform of the labour market, modifies the legal framework for the use of wage opt-out clauses aiming to make it easier to use them. According to the new law, following a consultation procedure, a company agreement between the employer and the employees' representatives might depart from the wages fixed by a higher level collective agreement, when, as a result of the application of those wages, the economic situation and prospects of the company could be damaged and affect employment. This agreement, which can only apply while the collective agreement

at a higher level has not exceeded its term or, in any case, for a maximum period of three years, must clearly determine the new remuneration to be paid and a schedule of gradual convergence towards the previously applicable wages.

In Ireland, derogations from sectoral agreements are not foreseen in the law and should, in principle, be dealt with by the bargaining parties themselves. However, the National Minimum Wage Act includes an ‘inability-to-pay’ clause. When an employer cannot afford to pay the NMW due to financial difficulties, an application may be made to the Labour Court which can, following an inquiry, exempt the employer to pay the rate for between three and 12 months. The employer must be able to demonstrate that the proposed exemption would be needed to preserve jobs and has the consent of a majority of the employees, who must also agree to be bound by the Labour Court decision. The Court determines, if applicable, the level of the wage to be paid by the employer during the period of the temporary exemption. In addition, in 2003–2009, the national social pacts, including national wage agreements included an inability-to-pay clause. The clause concerns employers that can prove that they are in difficult financial circumstances in which full payment of nationally agreed wage increases would mean serious loss of competitiveness and employment. If their application is successful, they can refrain from paying all or some of the pay increases due in a wage agreement. The recent collapse of the practice of national social pacts also means this clause has lost its relevance.

Finally, in Italy the possibilities to use opening clauses on wages have been widened as well through a social pact. Until recently, there were no specific regulations on opening clauses but in principle the possibility existed to include such clauses in sectoral collective agreements. However, in January 2009 the main employers’ associations and trade union confederations, but with the important exception of the largest union confederation CGIL (General Italian Confederation of Workers), signed the Framework Agreement for the Reform of the Collective Bargaining System (FARCB). The government supported the negotiation of this agreement and also signed it itself as employer for the public sector. The FARCB, among other things, permits company-level collective bargaining – or territorial level bargaining concerning specific regions or cities – to change, for the worse, the wage and other standards of sectoral collective agreements, in cases of ‘economic crisis, or to promote economic and employment growth’. However, the FARCB also leaves open broad possibilities for the sectoral social partners to control the specific conditions and procedures of such opening clauses, which they can specify in the sectoral agreements.

### 3. DEROGATION CLAUSES IN PRACTICE

There are large differences between the seven countries concerning the extent to which opening clauses and similar derogation clauses have been adopted in (inter)sectoral agreements and the extent to which they have effectively been applied at company

level. From the country studies it emerges that in Austria, Belgium, and Italy hardly any sectoral agreements contain opening clauses, and the existing opening clauses are hardly used in practice. In Austria, the only opening clauses adopted in the last decades were one in the metal-working agreement in 1993 and one in the electronics industry in 2009. The former concerned the possibility to use the agreed increases in actual wages for the promotion of employment and was used by 3% of the companies in the sector, employing 13% of employees. The latter, in response to the economic crisis, determined that the agreed increase of actual wages of 2.2% could be reduced to 1.4% in those companies which had suffered reductions in turnover of at least 15% during the first quarter of 2009. It was applied in 60 companies employing some 16.000 employees. Both clauses were short-lived however and were not renewed in the next agreement. In Belgium, in the period from 2005 until today, opening clauses dealing with wages appeared in sectoral agreements covering six (sub) sectors: engineering, metal manufacturing, food manufacturing, retail of food products, large retail stores and department stores. These sectors together cover only a small part of the Belgium economy and labour market. The opening clauses allow companies in economic difficulties not to implement the wage increases determined in the respective sectoral agreement (in some cases this includes the increases of the sectoral minimum wages), or deal with additional wage and labour cost elements such as premiums. Often, these clauses have been present in sectoral collective agreements since the 1990s, and are not a response to the recent economic challenges of the late 2000s. What is more, they are hardly ever applied at company level and the total number of companies using these clauses is estimated to be fewer than 10 per year. In Italy, an opening clause has existed only in the chemical-pharmaceutical industry where it was introduced in 2006. The derogations can concern in principle all aspects of pay except the minimum wage of the sector, which cannot be undercut. However, the clause has never been used at company level. Still, it remains to be seen if opening clauses will be used more in the future following the adoption of the FARCB.

In Spain, wage opt-out clauses allowing the (partial) non-implementation of negotiated wage increases were included in 51% of sectoral agreements, covering 74% of workers in 2009.<sup>3</sup> They largely concern possibilities to not implement negotiated wage increases. However, few companies actually use these clauses. A report from the Bank of Spain shows that when facing economic difficulties, only 4.6% of undertakings decide on using the opt-out clause to reduce wages, while 70% choose to dismiss workers.<sup>4</sup>

In France, after the adoption of the Fillon law, the relevant question is not which sector agreements include an opening clause but which include a clause prohibiting undertaking agreements to derogate for the worse from sectoral wage norms. Some

<sup>3</sup> Statistics Bulletin of the Ministry of Labour and immigration [www.mtin.es/estadisticas/cct/CCT09OctAv/cc1/index.htm](http://www.mtin.es/estadisticas/cct/CCT09OctAv/cc1/index.htm).

<sup>4</sup> Report of the Bank of Spain of 2009 cited by Pose Vidal (2009).

15% of sector agreements include such a clause (Combrexelle, 2008). In principle, the other 85% leave open the possibility of undercutting sector agreements at company level on those wage issues not exempted from the possibility of derogations by the law. However, an evaluation of the impact of the reform shows that no noticeable changes have emerged concerning the levels at which bargaining takes place (Dufour, 2008). Indeed, no noticeable increase can be observed in the use of company agreements and industrial relations actors continue to follow traditional bargaining practices, not undercutting sectoral wage agreements at company level.

The major outlier among the seven countries is Germany. Here all important sectoral agreements now contain opening-clauses. However, their content can vary widely. The wage issues they affect range from basic pay to bonuses but may also specify a list of issues on which derogations are possible. They can concern absolute reductions or rather derogations from agreed wage increases. Also, they sometimes involve postponement of the payment of the wage elements in question, a reduction or even a complete annulment in the case of bonuses, for example. Sometimes the use of an opening clause is restricted to a situation when a company is in serious economic difficulties; in other cases it can be used for improving general competitiveness. In exchange employees may be offered enhanced job security, such as a commitment by employers not to resort to compulsory redundancies over a defined period of time. And not only are opening clauses more widespread in Germany than in the other six countries, they are also used more frequently. According to the WSI works council survey, in 2010, 16% of establishments used opening clauses to set lower pay rates for job starters; 14% reduced or suspended annual bonus payments; 13% deferred agreed pay increases; and 9% cut basic pay.<sup>5</sup>

Finally, in Ireland the situation is slightly different, with its inability-to-pay clauses in the Minimum Wage Act and, between 2003 and 2009, in the national social pacts. No respective sectoral clauses exist. As to their use in practice, the clause of the Minimum Wage Act has never been used at all. The clause in the national agreement, however, has been used, although not abundantly. Between 2003 and 2008, in some 175 cases the clause has effectively been applied (the figure is an estimate based on data from the Labour Court since there is no precise administration of all cases in which this clause was used).

From this comparison it emerges that derogation clauses are only widespread in sectoral agreements in Spain (following their mandatory nature) and Germany, and that only in Germany they are widely applied at company level.

<sup>5</sup> See: [www.boeckler.de/510\\_109835.html](http://www.boeckler.de/510_109835.html).

#### 4. THE POLITICS OF DEROGATIONS

From the case studies it emerges that the issue of wage derogation clauses is a conflictual issue. It is put on the agenda first of all by the employers, who often see such clauses as a means to getting wage flexibility in a competitive global economy, and particularly in times of economic hardship, without having to dismiss workers they expect to need again once the crisis period is over. Also, wage derogation clauses fit the broader attempts by many employers' organizations to promote a more generalized decentralization of collective bargaining. This pressure has been the strongest in Germany, where the employers' associations have successfully pressed the case for an across-the-board policy of collective bargaining decentralization since the early 1990s. For some time they also supported demands for a change in the legal framework to allow companies to diverge from sectoral agreements but this position was abandoned more recently when the president of the Confederation of German Employers' Associations (BDA) acknowledged that the German bargaining system has now become so flexible using the existing legal framework that legal changes are no longer needed.

At the same time, employers' organizations rarely advocate a termination of (inter) sectoral bargaining practices and more often they advocate organized decentralization, i.e. increased company-level bargaining within the framework of rules and standards set by (inter)sectoral agreements.

Moreover, in a number of cases the governments play an important role in the emergence of derogations. As discussed above, in Spain and France legislative changes were made in recent years with the aim to facilitate lower company level wage deviations from those agreed at higher level. In Austria legal changes with the aim of decentralizing collective bargaining were proposed by the government in the early 2000s but remained limited to working time issues. In Italy, in 2009, the government sponsored and signed an inter-sectoral agreement that facilitates derogations at company and territorial level. And also in Germany the various governments of the last decade, as well as the major political parties, have strongly supported the decentralization of collective bargaining in general and the use of opening clauses in particular. For example, in 2003 the German Chancellor, Gerhard Schröder threatened with the introduction of a statutory opening clause that would apply to all collective agreements in all sectors.

The call for derogation clauses can also come from external actors. For example, in Belgium, neither the employers' organizations nor the government are seriously questioning the basic characteristics of the Belgian collective bargaining system and are not arguing for substantial modifications of this system. Pressure for decentralization of wage bargaining and the use of opening and related clauses largely comes from outside Belgium through the respective recommendations of international organizations, in particular the OECD (e.g. OECD 2007: 82–84). These recommendations do not find much resonance within Belgium however.

Trade unions are mostly against extensive decentralization and derogations from higher level wage agreements and in most cases try to oppose legislative changes facilitating such derogations, their inclusion in sector agreements and their use at company level. They often see them as a threat to the systems of collective bargaining and to the homogenization of wages throughout sectors. They also fear the weakening of worker protection, the increase of wage competition and a rise in the number of low paid workers. Their opposition is the major, although not the only, reasons why even in countries like Spain and France, where the legal context favours derogations, their use in practice is scarce. At the same time, in the case of specific companies in serious economic difficulties, trade unions are often ready to negotiate on measures to overcome these difficulties and maintain employment, even if this includes, for example, a temporary undercutting of higher level wage standards. However, they will always demand that such deviations are temporary and allow for some union control over their use. As a result, in all cases, the use of derogation clauses at company level require an agreement between the employers and the trade union, works council or other employee representative.

In Germany, trade unions have had a harder time than in the other countries to stand the combined pressure from employers and governments. They have been pressured to accept opening clauses by political threats to increase decentralization through legislative changes, as well as by declining union power. Initially they did so largely as a defensive reaction aimed at safeguarding jobs or preventing a relocation of operations. Given the seeming unavoidability and irreversibility of decentralization, unions like IG Metall have now shifted to a new strategy which aims to build organizational strength through a more assertive bargaining policy at company level.

Also, in some countries the trade unions are divided on these issues. For example, in Italy, among the main trade unions, CISL and UIL agree with the government and the employers' associations on the need for greater decentralization of collective bargaining with the aim of strengthening competitiveness and efficiency. Instead, the largest union CGIL insists on the importance of the national-sectoral level, which guarantees minimum standards to all workers, and calls for a strengthening of this level as well as the territorial level.

## 5. CONCLUSIONS

The inclusion of wage derogation clauses in higher level agreements and the practical use of such clauses at company (or sometime territorial) level is much debated in some of the seven countries studied here. In most of the countries here discussed, opening clauses have not had a major effect on the collective bargaining systems which have been remarkably stable. Ireland is, to some extent, an exception as recently

the practice of national agreements broke down. This was, however, not related to the question of opening clauses or a drive for decentralization. The major exception is Germany where the widespread use of collectively agreed opening clauses has triggered a process of decentralization that has shifted an increasingly large part of bargaining responsibilities to the company level. This has led to a significant loss of regulatory power on the part of both employers' associations and trade unions and once inviolable collectively agreed standards have become objects of re-negotiation at company level. As a consequence, unions have to engage much more directly with the needs and requirements of companies, and works councils have less scope to take refuge in the mandatory character of sectoral regulations when confronted by management calls for local concessions. The pressure from employers and the government for such decentralization has been stronger than the power of the unions to resist it. This, together with the declining coverage of collective agreements, has reshaped German collective bargaining profoundly.

In most other countries unions and employers are rather interested in maintaining stability or minor modifications to their collective bargaining systems, instead of thoroughly decentralizing wage bargaining. Also, trade unions are often successful in neutralizing pressures to increase the use of opening clauses. Moreover, both unions and employers generally prefer to use alternative mechanisms to overcome economic difficulties. These can be unilateral, like employers in Spain deciding not to renew temporary contracts. They can also be negotiated. For example, in a number of countries, agreements are making use of state programmes opening up possibilities for short time working arrangements and temporary unemployment. In this way they preserve jobs and most of the workers' income, while also temporarily reducing labour costs. The emergence of such negotiated, competition-enhancing and socially just solutions is greatly facilitated by state support. Also the increase of working time flexibility is frequently used to adjust to economic difficulties.

The resort to such alternative solutions is sometimes also motivated by the fact that applying opening clauses can be a complex and time consuming process which involves substantial paperwork as well as the disclosure of detailed information on a company's finances. In addition, the resort to opening clauses may result in complicated and conflict-ridden negotiations between inexperienced company-level actors. What is more, downward wage adjustments are often not considered the right cure for competitive problems, which are not necessarily related to wage costs but may derive from non-wage related factors such as the regulatory framework, the general economic situation, characteristics of the production system, or lack of skilled labour.