Study #2

From young to old and unemployed?

How older workers can remain in the labour market for longer without taking jobs away from young

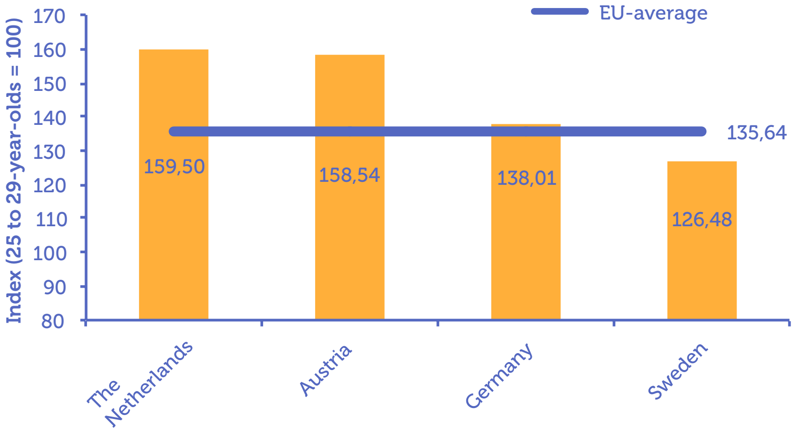
Michael Christl, Dénes Kucsera and Hanno Lorenz

Think Tank Agenda Austria

At a glance

It is difficult for older people to find work again after a period out of the labour market or after losing their job. This is something that all interest groups and political parties can agree on. One of the reasons for this is the high labour costs for older workers, and comparison of the salaries of 55- to 59-year-olds with those of 25 to 29-year-olds in many countries backs this up:

Wage of a full-time employee 2012 – Comparison of 55- to 59-year-olds with those of 25- to 29-year-olds



Source: OECD.

Note: Index of the relation of wages.

On average in the EU a person aged between 55 and 59 earns a gross salary that is 35 percent higher than someone aged between 25 and 29. In Austria the figure is 58 percent. (The Netherlands has introduced other measures to reduce the difference in salaries.)

But there is not much agreement on how to tackle the problem of unemployment amongst older workers. “Packing off” older employees into early retirement is becoming more and more difficult, as early retirement plans are expensive for the government. When this study was published, there was discussion about a bonus scheme to penalise companies with an especially low proportion of older workers – an idea that was met with criticism from some quarters.

This study firstly evaluates the strengths and weaknesses of the Austrian labour market with respect to older workers. It goes on to address regulation of the labour market, the labour cost and labour productivity, as well as financial incentives for early retirement.

It further looks at the ways other countries have successfully managed to achieve higher labour force participation rates of 55- to 64 year-olds. The table below gives an overview of measures taken abroad and their impact.

Reforms in the countries included in the study

Country	Type of reform	Description	Results
Germany	Increased labour market flexibility	Relaxation of employees' protection against dismissal, stricter qualifying criteria for unemployment benefit and shorter entitlement periods.	Germany's labour market functions effectively, not only with respect to older workers.
The Netherlands	Experience rating	Contributions to the incapacity benefit system have been split into a fixed and a sector-specific share. Companies with higher invalidity rates pay higher contributions on the basis of the cost causation principle.	The more effective prevention measures in place in the Netherlands go a long way to explaining the smaller number of people drawing invalidity pensions.
Sweden	Pension reform	Changeover from a defined benefit pension system (similar to the Austrian one) to a defined contribution system.	The pension system is financially sustainable and fair to different generations. Financial incentives to encourage people to extend their work life have also been successfully introduced. There is now flexibility with respect to when people decide to retire.
	Reduction in seniority-based pay	Seniority-based pay was abolished for civil service jobs in the 1990s and replaced by a performance-based system of remuneration.	There are no countries with a higher rate of employment for the older section of the working population than Sweden.

Source: own research

In Germany, for example, the introduction of measures to increase the average retirement age has made early retirement less financially attractive, as this now means significantly reduced pension payments. The Hartz reforms are also part of the reason that more older people are in work and can find jobs, as unemployment has decreased within this group. As a consequence, the global economic and financial crisis has had little effect on the German labour market.

In the Netherlands incentives to take early retirement were removed in the 1990s – a process in consent with the labour unions. General practitioners no longer decide on qualification for retirement on the grounds of incapacity, as this is now the remit of an independent authority. At the same time companies are also responsible for a proportion of the pensions paid to employees who retire due to incapacity, and therefore are incentivised to introduce preventative measures. Employers pay no social insurance contributions towards the incapacity benefit system for new employees over 50 who were previously unemployed or claiming incapacity benefits, as well as for existing employees who are aged over 62. Employers also pay significantly less, or nothing at all, for older workers during probationary periods, as these new members of staff continue to receive social security benefits. Workers aged between 62 and 67 get a tax bonus for remaining in the labour market, and job seekers over 57 have to prove that they are actively seeking work in order to qualify for unemployment benefit. The long period of entitlement to unemployment benefit has also been reduced.

The major reason that Sweden has a high labour force participation rate for older people is that the pension system provides a strong incentive for this group to remain in the labour market. Unlike in Austria, payments are linked to the estimated length of time that pensioners will receive them. Job seekers' employment benefit is reduced for two months if they turn down an offer of work that the authorities consider to be suitable. Claimants who refuse three such offers lose all entitlements. Legislation protecting long-serving employees against redundancy proved to be problematic and was therefore relaxed. Another significant factor in creating employment opportunities for older people over the long term is that, in comparison to Austria, aged-linked compensation is not very widespread: salary curves are quite flat, meaning costs for employers increase relatively little as their age-wage profiles.

Our recommendations for Austria are based on these examples. The study also puts the popular argument that older workers are taking jobs away from the young to bed. The empirical findings show that higher rates of employment amongst older people actually tend to result in higher rates of employment for the young. This is because if more people are in work, then purchasing power increases, which in turn fuels consumer demand that creates jobs.

What action should be taken to provide older workers with better opportunities in the labour market so that a higher share remains in employment?

- Like in Sweden, older people should be given the chance to extend their work life. In order to achieve this, rising life expectancies have to be factored in to the pension system so older workers will be financially better off if they keep working. Agenda Austria also advocates the introduction of part-pension payments based on the Swedish model. If Austria had a pension system that was similar to Sweden's, then it would be possible for pensioners to work part time while claiming a part of their pension entitlement – a transparent system that would not incur any additional costs.
- Agenda Austria recommends weakening the seniority-based pay in collective bargaining processes. This will not change total career earnings as, compared to age-linked pay, workers will receive higher salaries at the beginning of their careers to compensate for the relatively low salaries at the end. The link between pay and age is a hangover from a time when it was usual to remain at the same company or organisation for an entire career: a low initial salary was made up for by the same employer with higher pay later on. Today people are changing job frequently and age-linked compensation is counterproductive, and in many cases an obstacle to finding a new job.
- Other countries have managed to make it easier for companies to compensate older employees on the basis of their productivity, and this should be possible in Austria, too. It is not uncommon that an employee's productivity decreases with age, while the cost to the employer actually rises. The principle should be "performance not age", making it possible to reduce a worker's salary without employers having to resort to special procedures to make them redundant and then re-employ them (Änderungskündigung). There must be alternatives to this practice, and it should not be redundancy.
- The high degree of protection against redundancy for older employees is counterproductive and should be reduced. This protection makes it hard for older workers to find new jobs if they are made redundant following a company closure. If pay for older members of the labour market falls to lower levels (by weakening the link between salary and age), companies will have more incentive to hire and retain older, more experienced workers.
- We are of the opinion that an experience rating system based on the Dutch model is worthy of consideration. Under such a system, part of the cost of an incapacity pension falls on the party responsible: employers in sectors with high rates of incapacity will have to pay higher social insurance contributions.