THE EMPLOYERS' MANIFESTO
2011—2015

Asutatud 1917
TÖÖANDJATE KESKLIIT
ESTONIAN EMPLOYERS' CONFEDERATION

FOREWORD

Dear Reader

Today we are announcing a renewed four-year action plan for the Estonian Employers' Confederation. "The Employers' Manifesto 2011–2015" is the second of its kind programme document where the Council of the Employers' Confederation identifies the objectives which will guarantee the sustainable economic growth. Similarly to the previous programme document, which is coming to an end (Manifesto 2007–2011), the objectives are grouped into five areas: state administration and economic policy, labour market, taxation, education and social protection.

On 6th March 2011 the members of the next Riigikogu will be elected. Consequently, the Employers' Manifesto is primarily aimed at them, but it is also open for discussion to trade unions, citizens' associations, other interest groups and to wider public in general. The proposals made in the Manifesto are carried by the wish to raise the competitiveness of the Estonian economy as this forms the basis of the wellbeing of the society.

We announced the previous manifesto in January 2007 to celebrate the 90th anniversary of the Estonian Employers' Confederation. The proposals we made then grew out of our concern over the future of the Estonian economy. In 2008 we entered the economic crisis, which forced the whole society to adopt austerity measures and the tax burden was raised as well. And yet, despite the crisis, we managed to achieve some important landmarks for the economy: we will join the euro zone on 1st January 2011, amended the out-dated labour legislation and improved labour market services, and raised the retirement age.

We hope that the objectives of this Employers' Manifesto will be met to the same extent.

Enn Veskimägi
President

Tarmo Kriis
Chairman

Tallinn, 30th August 2010

VISION FOR 2020

Ten years is a long enough period to carry out significant changes in almost any areas of life, as well as to achieve first results. We wish that the development until 2020 would bring along a quick rise in living standards, reaching at least 90% of the EU countries' average. In order to achieve this, the average annual real growth over the period will have to exceed that of the EU average by 4 percentage points. The rapid economic growth will be based on the development of export, rooted in a more open economy and society and the internationalisation.

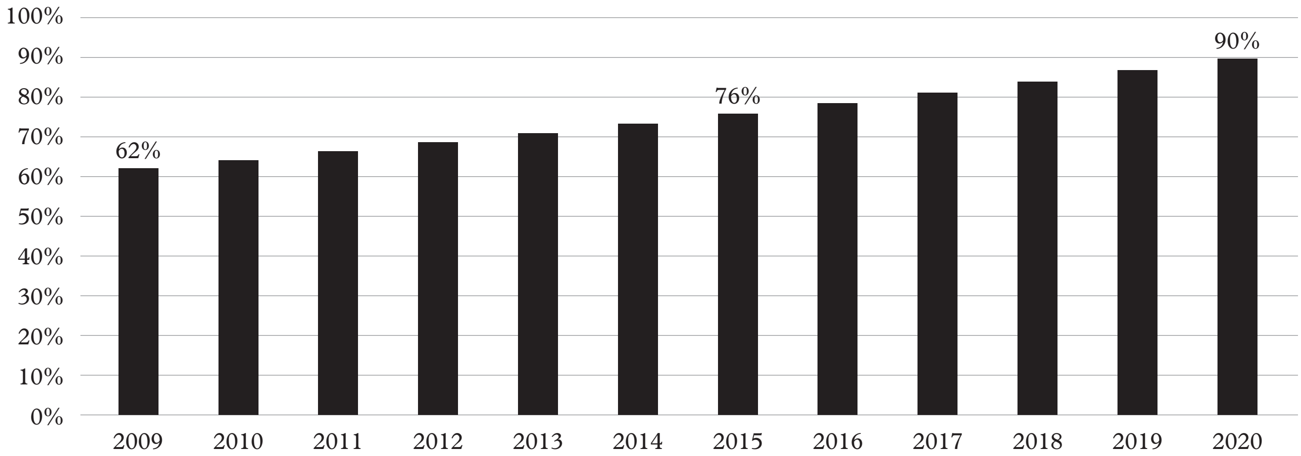

Figure 1. Estonia's GDP per capita (in PPP units) in relation to the average of EU27 on an assumption that our growth exceeds EU27 on average by 4 percentage points. *Source: EU Autumn 2009 forecast, calculations by the Estonian Employers' Confederation (ETTK)*

Estonia is a highly efficient country with a low tax burden. Being part of the euro zone and our low public spending has generated more trust in the Estonian economy. As a result, the business sector's access to capital has improved significantly. The work in the public sector has become more efficient through the substantive development of e-services, the extensive collaboration with the private sector, the involvement of international competency and a performance related personnel policy. The growth of productivity has improved the competitiveness of the Estonian labour force – the productivity growth exceeds the salary growth. The employment has reached the 2008 pre-crisis rate.

In the structure of the economy there has been a shift to higher added value business activities. The development of information technology, flexible labour relationships and forms of work, as well as increased levels of knowledge and skills are the essential contributors to achieving long-term competitiveness. The young people of Estonia are competitive due to good education and active work habits, and the competitiveness of adults has improved with the help of state subsidised life-long learning. The development of businesses is no longer inhibited by lack of skilled labour – employees with required qualifications can be hired from Estonia or from abroad if necessary. The working environment is safe and it places value on the employees' health. The increased life expectancy has extended the duration of the working life.

"The Employers' Manifesto 2011–2015" lists the proposals for the next four years, which will help to achieve the stated objectives.

I

State administration and economic policy

1. From 1st January 2011 Estonia will be the member of the euro zone. Estonia will participate in developing and applying the policies that will ensure the stability of the euro zone. In order to ensure the stability of euro, it is necessary to continuously monitor the fiscal policies of the euro zone countries, to intervene immediately if a breach of the budgetary discipline has taken place, and to impose more stringent sanctions to countries that consistently fail to meet the budget criteria.

2. Estonia's fiscal policy has to set an example to other euro zone countries. To ensure the macro-economic stability, the fiscal policy has to be contracyclical: instead of increasing social expenditure when the times are good, and burden the private sector with budget cuts and raised taxes when the times are bad, we suggest that sufficient budget surpluses have to be kept throughout economic growth periods; this would avoid overheating of the economy and ensure reserves for times of economic downturn. The fiscal policy will have to be the tool that helps Estonia to continue meeting the Maastricht inflation criteria.

3. The total spending of the government sector in relation to gross domestic production has to be among the three lowest figures among the euro zone countries. The same recommendation applies to the level of taxation and public debt.

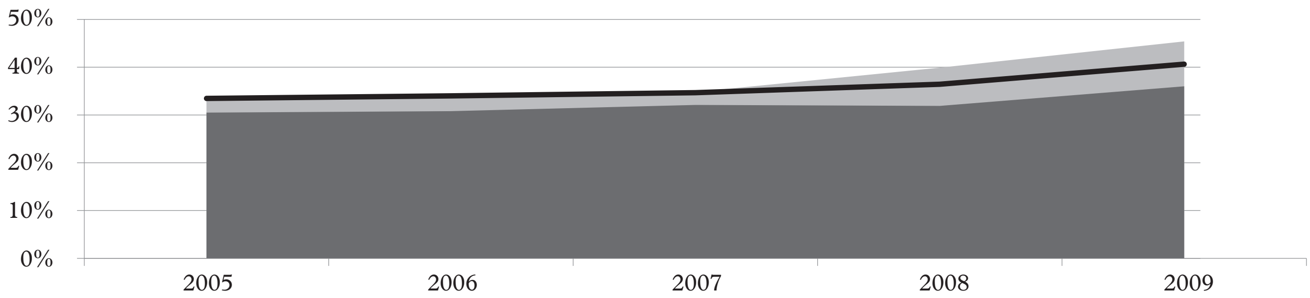

Figure 2. Tax revenue and government sector spending in relation to GDP. *Source: Eurostat, calculations by ETTK*

- Tax revenue, Estonia
- Government sector spending, Estonia
- Government sector spending, the average of 3 lowest spending EU countries

4. One of the preconditions of achieving the required fiscal policy is an extensive reform of the government sector – reduction of public sector operation costs along with improved accessibility of public services. The essential parts of the reform are listed here:

    a. offering as many public services as possible as e-services;

    b. reducing the number of state institutions and continued consolidation of their functions, reducing numbers of state officials, buying in state support services from the private sector, and rotation of civil servants between state offices and between state offices and the private sector;

    c. reducing operational costs of local governments by reorganising them into bigger units, also improving the quality of public services they offer to local communities (e.g. child care, public transport, infrastructure maintenance) and following the financial discipline. Services offered by local governments must, among other things, be sufficient to guarantee suitable labour force for enterprises and other conditions for developing business outside Tallinn city and the surrounding Harju county. The funding principles of local governments must be changed to increase their interest in creating new businesses and jobs.

5. The quality of impact analyses for national development plans, legislation (especially state budget act) and policy changes has to improve significantly. Before adopting any changes the substantive impacts of these changes on impacted parties, as well as the economy and society as a whole, must be thoroughly analysed and explained. In order to achieve an efficiently functioning regulation, it is necessary to systematically include private sector competence (incl. the Employers' Confederation and its members) in formulating policies.

6. Public sector investments must be directed primarily at measures that improve the competitiveness of the economy (especially at infrastructure objects and services that promote labour force accessibility and investments in enterprise and improve foreign links). Priority should be given to securing flight and train connections with strategically important locations for Estonia, as well as to update the border crossing infrastructure with the Russian Federation.

7. When supporting enterprises from structural funds we must avoid an overly fragmented and unsystematic approach, and should direct the funds increasingly at things that help create added value – constructing infrastructure objects, increasing industrial output and supporting export (incl. tourism sector). Funding from structural funds must result in real growth of productivity (i.e. avoid creation of fixed costs that do not add value).

8. The main objectives of the foreign economic policy must be to increase direct foreign investments in the Estonian economy, to open Estonian enterprises to foreign investors and to assist Estonian entrepreneurs more in opening new markets for them. The Estonian state has to stand up more for the opportunities of Estonian enterprises to offer services in other countries. Even more support in the form of advice and consultations should be made available to the Estonian enterprises who face obstacles to free movement of services in foreign countries. Among other things, the state has to substantially improve the availability of information about Estonia and on applying for Estonian visas for foreign citizens. For this purpose Estonia should maximise the presence of foreign missions of other European Union states.

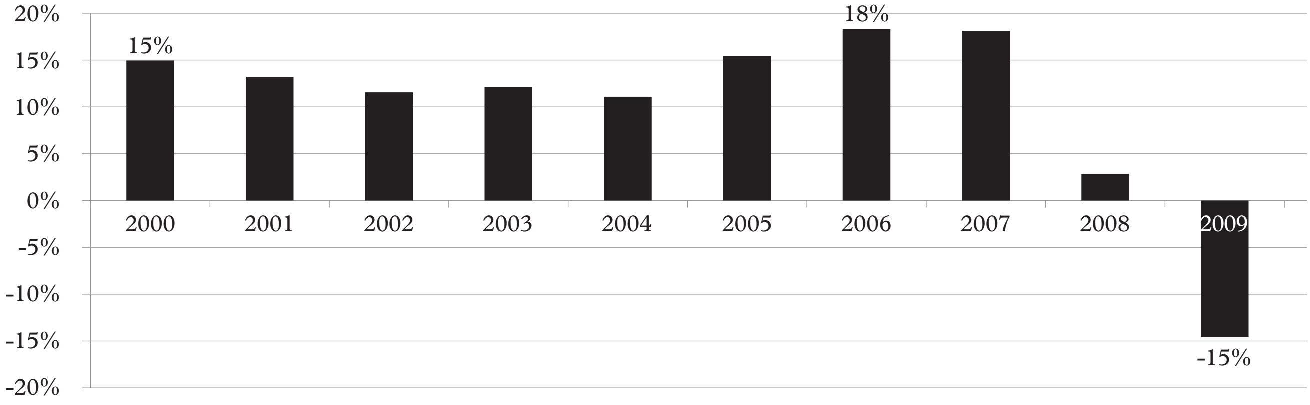

Figure 3. Changes in the flow of direct foreign investments into Estonia *Source: Bank of Estonia, calculations by ETTK*

9. Joining the euro zone will create a significantly better foreign economic policy platform for improving the economic relations with our neighbours, incl. the Russian Federation, with the most urgent issues that need solving being the boarder agreement, double taxation agreement and protection of investments agreement. It is necessary to conclude double taxation agreements with the important trade partners of Estonia with whom there is currently no agreement (e.g. the Republic of Kazakhstan).

10. Estonia has to actively support the formulation of the European Union industrial policy.

II

Labour market

1. In order to improve the level of employment, the development of various forms of flexible working should be promoted – such as, part-time work, telework and temporary agency work – , thus bringing to the labour market the knowledge and skills of those people who for any reason cannot work in traditional forms of working or whom employers cannot hire full time. In addition, the long-term unemployment can be brought down and the less employable people re-introduced to the labour market by lessening the impact of labour taxes and the minimum wage requirement.

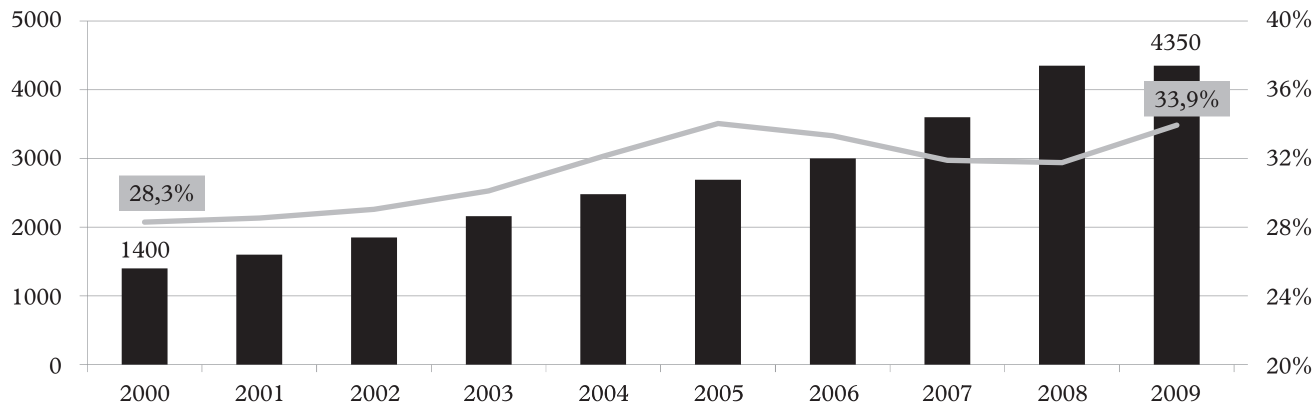

Figure 4. Minimum wage in Estonia as compared to the average wage.
Source: Statistics Estonia, government regulationsmäärused

Minimum wage (EEK) (left-hand scale, l.s.)
Ratio of average wage to minimum wage (right-hand scale, r.s.)

2. The second stage of the unemployment insurance system reform has to be carried out to give the Estonian Unemployment Insurance Fund the right to offer active labour market services from its insurance funds and the complete decision-making authority to manage its budget accordingly. The unemployment insurance premiums must not be increased. The budget of the unemployment insurance has to be in surplus and its reserves must guarantee that a sudden rise in unemployment does not create pressure to raise unemployment insurance premiums.

3. Labour market flexibility is an essential factor in a country's financial stability in the euro zone. In the absence of an independent monetary policy, the labour market's ability to adapt adequately (devaluation) is critical in periods of economic downturn. Labour legislation must therefore allow for flexibility to lower labour costs during a recession, i.e. offer the employer better opportunities to reduce both working hours and pay in economically difficult times.

4. The public service must be reformed to ensure competitive parity on the labour market for private and government sector employers. The majority of current civil servants should be employed in accordance with the Employment Contracts Act, the headcount of civil servants must be cut and the rigid career models should be abolished in most cases. The wages of civil servants must not exceed private sector wages for comparative qualifications. The civil servants' special benefits, such as unreasonably high redundancy pay and long holidays, must be abolished.

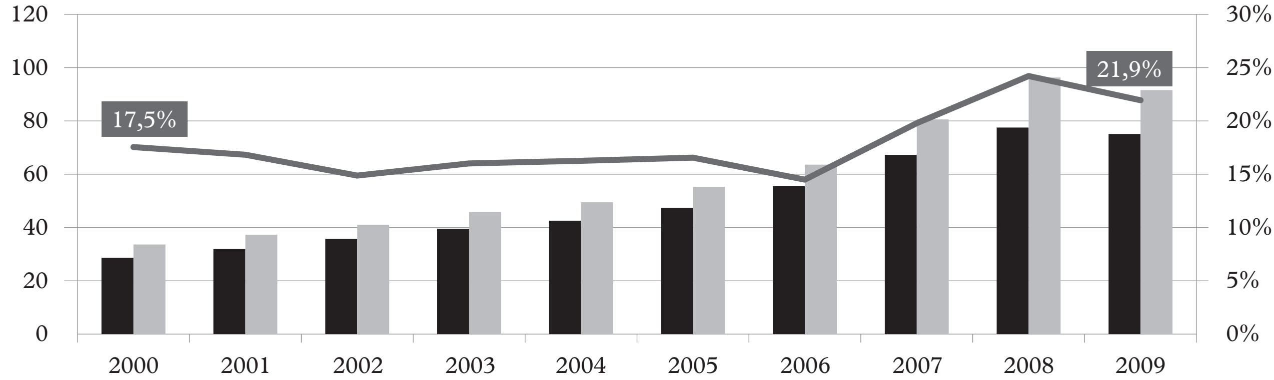

Figure 5. Average gross hourly wage in public administration and in Estonia on average. *Source: Statistics Estonia*

5. In order to avoid the local labour force becoming less employable, Estonia's labour market must be opened to foreign labour from third countries. It's especially important for higher qualification labour but, if necessary, short-term labour for low paid jobs (e.g. seasonal or unskilled jobs) should also be promoted. Since cheaper foreign labour used for short-term jobs would not affect the employability of Estonian workers on the labour market, it would be expedient to lower the prescribed average wage requirement on short-term jobs.

6. In no circumstances should signing a collective agreement be promoted before the employer is given an opportunity to free themselves of the conditions of the expired collective agreement. In addition, the collective employment regulation has to be supplemented with a principle that in case of signing a collective employment contract the obligation to refrain from striking applies to all issues and not only those agreed in the agreement.

7. The regulation on allowing strikes needs changing. The possibility of organising support strikes must be removed from the law since they are not directed at influencing work related decisions of their employer and since the company involved in a support strike has no legal possibility to act to avoid such labour disputes. A partial or total striking ban should also be applied to areas where indispensable production or service capacity has to be retained during a strike.

8. The role of the labour dispute committee in administrating justice as an extrajudicial body is problematic. It must be made possible to take an individual or a collective labour dispute to an arbitration tribunal.

III

Taxation

1. A stable tax system is of great value to the business environment. The tax system does not therefore need principal reorganisation or new types of tax, but lower tax burden instead. It would also benefit from a longer term future perspective, especially in regards to rising environmental taxes.

2. The corporate tax system in Estonia has enabled companies to create reserves which are essential in adhering to a contracyclical budgetary policy. At the same time, the benefits of the existing system are often not clear at a glance to foreign investors. In order to promote foreign investments it is necessary to apply a lower rate of tax on dividends, as dictated by a growing tax competition.

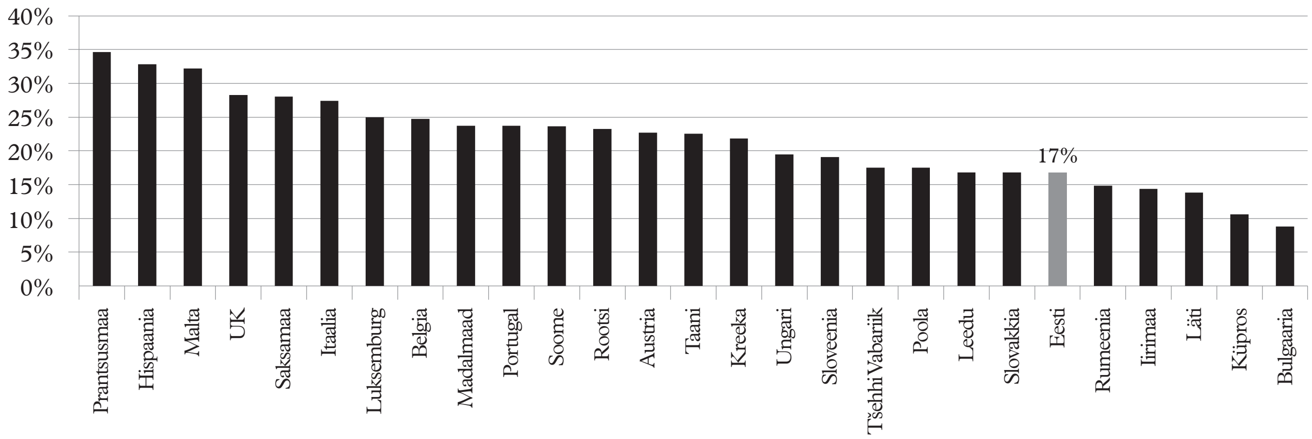

Figure 6. Effective corporate tax rate 2008 *Source: Statistics Estonia, government regulations*

3. In order to remain competitive we must keep lowering the level of labour taxes. Continued reduction of personal income tax is the primary catalyst to increasing employment. The rate of social tax on Estonian enterprises is one of the highest in the EU, which is a significant obstacle to involving foreign investment in the Estonian economy. The creation of higher added value jobs would require an introduction of a social tax ceiling in the current social tax regulation, which could be a sum calculated on three average statistical monthly wages as a maximum. Based on the practise of other countries, employees should become responsible for paying their social tax (similarly to income tax).

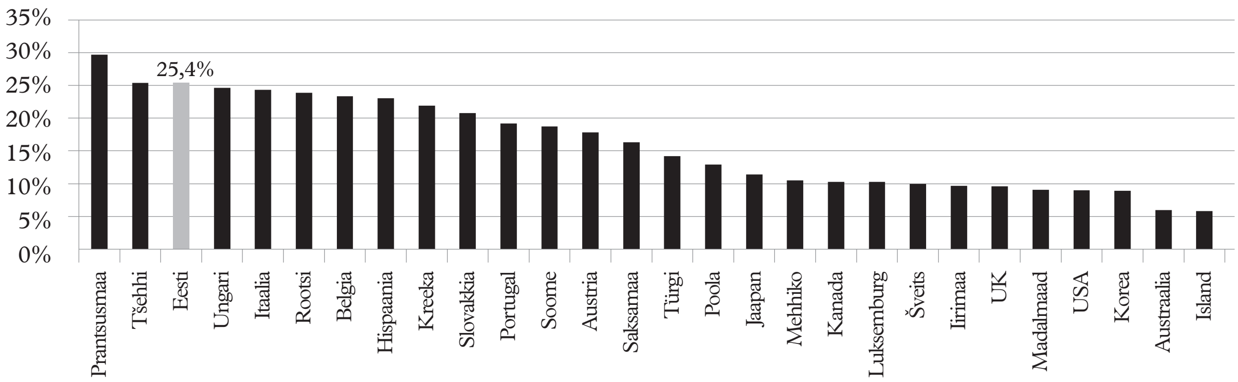

Figure 7. Employer's labour taxes/payments in OECD countries in relation to labour costs in 2009 *Source: OECD Taxing Wages 2009*

4. Entrepreneurial activity remains low in Estonia. Earning income from business should therefore be favoured above income from employment and should consequently be taxed at a lower rate.

5. In order to promote entrepreneurs' investment in human capital, the employer's investment in an employee's adult learning or health care should no longer be taxed as fringe benefit. Every effort should be made to promote employees' participation in company's success through profit sharing schemes. It is not prudent or justified to levy high tax on employees' share options.

6. High levels of excise duty have resulted in the extensive growth of the shadow economy in the trades of fuel, spirits and tobacco products. In order to alleviate the impact of high excise duties on free competition the surveillance activities must become considerably more stringent, or the excise duty rates must be lowered. The excise duties will not be raised during this programme period since this would result in empowering the shadow economy and increasing the cost of living.

7. The local government rights to levy local taxes and duties must be restricted. As a priority, the sales tax must be abolished and the land tax duty must be reduced.

IV

Education

1. The Estonian education system does not offer the labour market sufficient numbers of specialists with high professional qualifications. The situation will only improve if each and every educational establishment – from primary schools to universities – contributes to the process.

2. The biggest problem looming in education is the excessive size of school networks, which has become the main obstacle for the education reform. In order to change the situation the education funding principles must be changed so that the learner's interests prevail over those of the school. In general education, this would mean separating primary schools from upper secondary schools and closing down uncompetitive upper secondaries. Tuition fees should be introduced in higher education, supported by a scholarship system for more talented students or those from less privileged backgrounds. The scholarship system should encourage studying currently less popular sciences and technology.

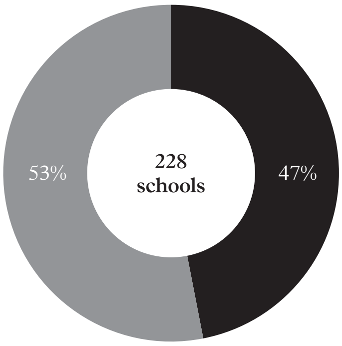

Figure 8. Division of 228 upper secondary schools by number of pupils in school year 2009/2010

More than 120 pupils
Less than 120 pupils

Source: The Ministry of Education and Research, calculations by ETTK

3. Internationalisation should be utilised to a greater extent to enhance the competitiveness of higher education – to bring fresh talent to Estonian universities, both lecturers and students, and to enable the majority of Estonian students to study in foreign universities with the help of scholarships. Foreign students (incl. from third countries) should also qualify for a chance to study under favourable conditions at the expense of the state and offered other measures to support later residency (e.g. residence permit under favourable conditions).

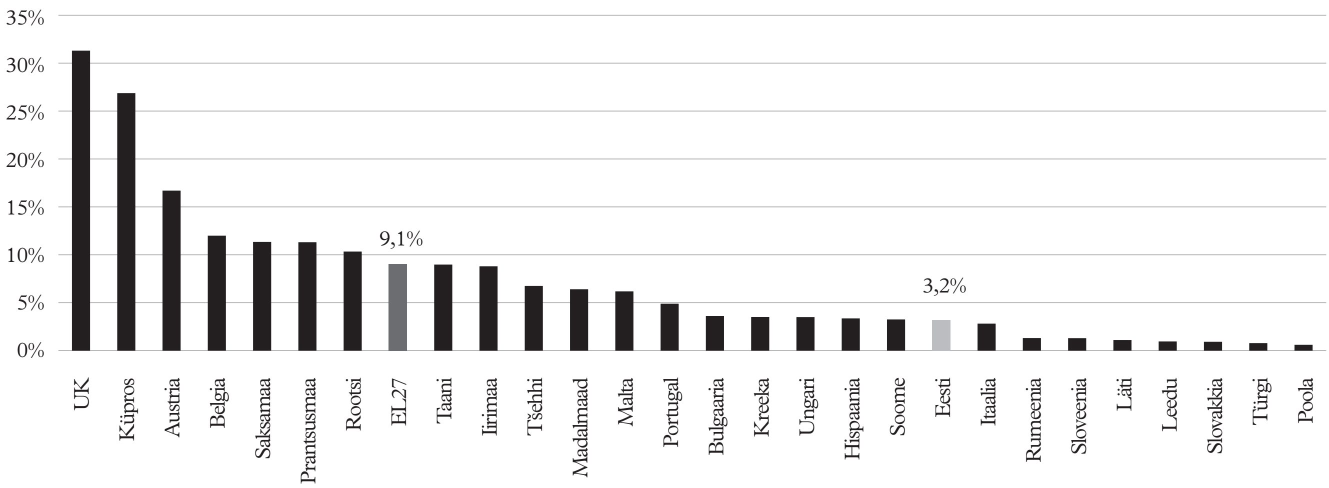

Figure 9. Share of foreign students among people studying in higher education in 2007 *Source: Eurostat, calculations by ETTK*

4. The state budget must finance retraining of the unemployed in formal education to increase the pool of people with professional qualifications.

V

Social protection

1. The health insurance should follow the principle that insurance costs are covered by those who carry the risks. The health insurance has to become a type of insurance funded from the employee's gross wage, which is a prerequisite to the employer covering the insurance costs for occupational accidents and disease. The reform would comprise of two stages:

a. the health insurance part of the social tax is switched to a tax borne by the employee; in addition, the health insurance is split into a solidary insurance component and a personified insurance component.

b. the insurance costs against damages caused by the working environment will be covered by the employer if the health insurance reform is carried out.

2. The main challenge for an ageing society is the adequate funding of pension funds. Estonia should set a target whereby the existing social tax would cover the growing numbers of old-age pensioners without the need to raise the tax rate. The following measures would help to achieve it:

a. the national retirement age must be increased on par with increased life expectancy to at least 67;

b. it is worth considering the question to which extent it is justified to pay a working pensioner a full state pension while they are working. An analysis is required on whether the input of the elderly to the labour market can be ensured through less costly means in a situation where there is a great shortage of work in the country;

c. the state pension indexation system must be changed so that when social tax revenue and consumer prices go down the pensions would come down too;

d. special pensions, superannuated pensions and old-age pensions under favourable conditions should be abolished. These must be replaced by insurance schemes based on voluntary pension contributions.

3. The principles of existing social benefit payments should be systematically corrected to ensure the benefits are not paid to people who have no real need for them.

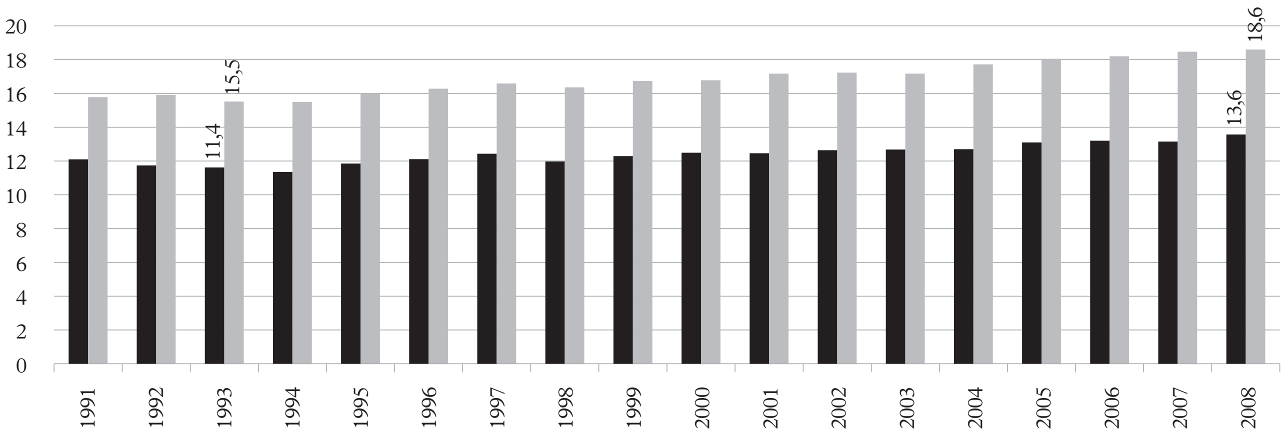

Figure 10. Life expectancy of 65-year-old men and women Men (years) Women (years)
Source: Statistics Estonia

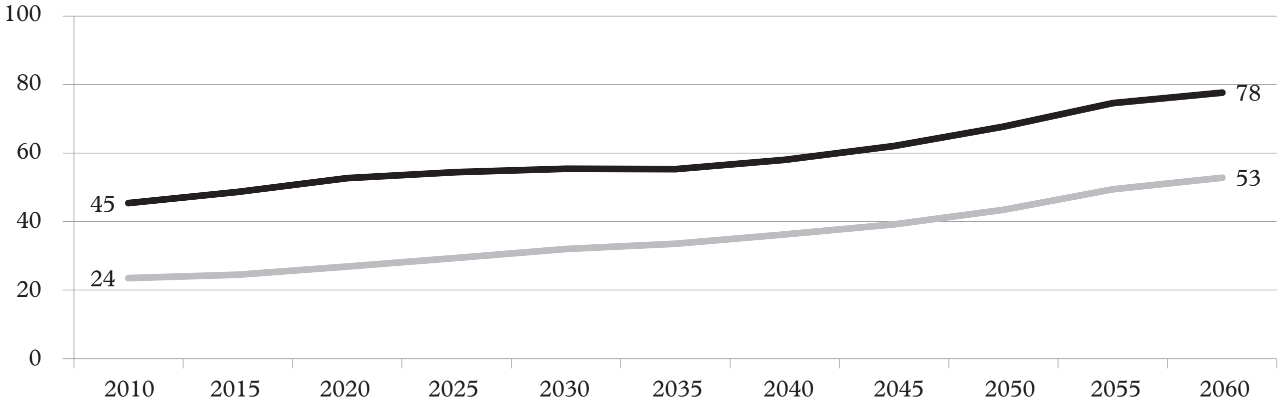

Figure 11. The number of dependants per one hundred working age residents. *Source: Eurostat, calculations by ETTK* Rate of dependants Rate of old-aged dependants

*The rate of dependants is the number of non-working age residents (aged 0–14 and 65+) per 100 residents of working age (aged 15–64).
**The rate of old-aged dependants is the number of residents aged over 65 per 100 working age residents (aged 15-64).

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AUGUST 2010